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A TREATISE
ON THE
BANKRUPTCY LAW
of the United States

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REMINGTON ON BANKRUPTCY

CHAPTER XXX.

TRUSTEE'S TITLE AND RIGHT TO ASSETS.

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- § 1493. Third Branch of Trustee's Peculiar Title and Rights Conferred by Bankruptcy Act—Fraudulent Transfers within Four Months.
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- § 1524. Staying Discharge and Permitting Creditor to Take Judgment to Fix Liability on Surety.

§ 1137. Complete Statement of Trustee's Title and Rights.¹—The subject of the trustee's title and rights to assets is threefold; the trustee succeeds to the bankrupt's title and stands in his

1. Bankr. Act, § 70 (a): "Title to Property."—"The trustee of the estate of a bankrupt, upon his appointment and qualification, and his successor or successors, if he shall have one or more, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt, as of the date he was adjudged a bankrupt, except in so far as it is to property which is exempt, to all (1) documents relating to his property; (2) interests in patents, patent rights, copyrights, and

trade marks; (3) powers which he might have exercised for his own benefit, but not those which he might have exercised for some other persons; (4) property transferred by him in fraud of his creditors; (5) property which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him."

See Bankr. Act, §§ 70 (e); 67 (a); 67 (b); 67 (c), (d), (f); 60 (a), (b); 47 (a) (2).

shoes and has the bankrupt's rights and remedies; and he also takes the property, in cases unaffected by any fraud of the bankrupt towards creditors, in the same plight and condition in which the bankrupt held it and subject to all equities and rights imposed upon it in the hands of the bankrupt, except where there has been some transfer or encumbrance of the property or seizure of it by legal process, void as against the trustee by some positive provision of the Bankrupt Act, although, as to the property coming into the custody of the bankruptcy court, he takes it in such plight and condition only to the extent that some creditor would have taken it had such creditor held a lien by legal or equitable proceedings thereon, and, as to the property not in the custody of the bankruptcy court, held an unsatisfied execution.

But in cases affected by the fraud of the bankrupt towards creditors, as also where there has been some transfer, encumbrance, or holding of the property void as to the bankrupt's creditors or inuring to their benefit by State law, for want of record or otherwise, the trustee succeeds to the rights of any creditor already qualified by State law to avoid the transfer, encumbrance or holding or who would be qualified thereby had such creditor as to the property in the custody or coming into the custody of the bankruptcy court, held a lien by legal or equitable proceedings thereon, or, as to the property not in such custody, been a creditor holding an execution duly returned unsatisfied, even though in fact no creditor may actually hold or have held such lien or execution.

And in addition thereto the trustee has the peculiar rights conferred by the special provisions of the Bankrupt Act, to avoid preferential and fraudulent transfers and liens obtained by legal proceedings within the four months preceding the bankruptcy.

Thus the trustee has the bankrupt's rights, title and powers, and is subject to his liabilities so far as a creditor would be subject thereto; he has the rights and remedies of creditors under the State law, both such as any existing creditor actually has asserted or is in position to assert and also such as any creditor might have had had such creditor become "armed with process" at the time of the bankruptcy; and he also has the peculiar rights conferred by the Act for the recovery of preferences and the nullification of liens acquired by legal proceedings within the four months before the bankruptcy.

§ 1138. Section 70 (a) to Be Construed with Cognate Sections—Trustee Gets More than Bankrupt's Title and Rights.—The statute, in § 70 (a), declares that the title taken by the trustee is the title the bankrupt had, but this clause must be read in conjunction with other sections of the statute and with two other parts of the same section,

otherwise a wholly insufficient idea of the complete title and rights of the trustee will be had.²

It is true the title which the trustee takes is that of the bankrupt. But his rights are those of the bankrupt and more. He has, by the positive provisions of the Act, the further rights which any creditor had by State law at the time of the bankruptcy, to set aside fraudulent transfers or liens and to expose the resultant title of the bankrupt.

Thomas v. Sugarman [even before Amendment of 1910], 19 A. B. R. 509, 157 Fed. 669 (C. C. A. N. Y.): "The complainant as trustee, however, represents not only the bankrupt alleged to be a party to the fraud, but his creditors who are innocent, and he may assert on their account rights against Sugarman, which the bankrupt could not."

In addition thereto he has the special rights conferred by the bankruptcy law itself in protection of the insolvent estate and its preservation as a fund for the benefit of all creditors, namely, the peculiar rights of avoiding preferential transfers and liens obtained by legal proceedings within the four months preceding the bankruptcy.

That the trustee's rights are not and never have been restricted to those of the bankrupt will become evident as the subject is developed. Indeed, had it not been so, the Bankruptcy Act would have been a menace to the commercial community instead of a safeguard of it; for upon bankruptcy the remedies available to creditors are suspended and are superseded, with certain exceptions, by those available to the trustee. Thus (except in certain exceptional circumstances) the creditors may no longer pursue the debtor's property in their own right; therefore, it would have been most disastrous had the trustee not been given the right to continue the pursuit of it in the ways that were being availed of by creditors at the time of the bankruptcy.

Beasley v. Coggins, 12 A. B. R. 358, 48 Fla. 215: "Section 70 (e) was intended to provide simply that the trustee in bankruptcy should have the same right to avoid conveyances as was possessed by creditors, or any of them, and this with especial reference to the Statute of 13 Elizabeth. Under the Bankruptcy Act, when one is thereunder adjudged a bankrupt, creditors are not permitted to attack fraudulent conveyances of their debtor, made more than four months of the adjudication of bankruptcy; and, if the trustee could not do so, then the act would constitute a device to permit fraudulent conveyances to take effect with impunity, in case they are successfully concealed for the specified four months. It is only by holding that the trustee is subrogated to the rights of creditors against a fraudulent conveyance that full effect and operation can be given to the Statute of 13 Eliz. against fraudulent conveyances, from which our statute is substantially taken."

In *re Garcewich*, 8 A. B. R. 152, 115 Fed. 87 (C. C. A. N. Y.): "It is not the meaning of the present Act that the institution of proceedings in bankruptcy

² In *re Thorp*, 12 A. B. R. 202 (D. C. Va.); impliedly, *Fourth St. Nat'l B'k v. Millbourne Mills Co.*, 22 A. B. R. 442, 172 Fed. 177 (C. C. A. Pa., affirming *In re Millbourne Mills Co.*, 20 A. B. R. 746, 162 Fed. 988).

should secure immunity to the title of fraudulent vendors or mortgagors, and deprive creditors of a resort to property out of which, but for the proceedings, they could have satisfied their claims,"

This clause 70 (a), then, giving the trustee, by operation of law, the bankrupt's title, should be read in conjunction with certain other parts of the statute, namely, in conjunction with subdivision, or rather class (4), of the same clause of this § 70, giving the trustee title also.

"to all property transferred by him [the bankrupt] in fraud of his creditors."

Also in conjunction with clause (e) of § 70, authorizing the trustee to avoid any transfer by the bankrupt of his property which any creditor of such bankrupt might have avoided, which reads as follows:³

"The trustee may avoid any transfer by the bankrupt of his property which any creditor of such bankrupt might have avoided, and may recover the property so transferred, or its value, from the person to whom it was transferred, unless he was a bona fide holder for value prior to the date of the adjudication."

Also in conjunction with class (5) of § 70 (a):⁴

"Property which at the time of the filing of the petition, the bankrupt could by any means have transferred or which could have been levied upon and sold under judicial process against him."

In *re Garcewich*, 8 A. B. R. 152, 115 Fed. 87 (C. C. A. N. Y.): "Section 70 declares in express terms that the title of the bankrupt shall vest in the trustee to 'all property which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him.' That language is sufficiently comprehensive to vest the trustee with title to all property of the bankrupt as against the fraudulent title of another."

And in conjunction with clause (a) of § 67⁵ which provides that:

"Claims which for want of record or other reasons would not have been valid liens as against the claims of any creditor of the bankrupt shall not be liens against his estate."

And in conjunction with clause (b) of § 67, which reads:⁶

"* * * whenever a creditor is prevented from enforcing his rights as against a lien created or attempted to be created by his debtor, who afterwards, becomes bankrupt the trustee of the estate of such bankrupt shall be subrogated to and may enforce such rights of said creditor for the benefit of the estate."

3. *Fourth St. Nat'l B'k v. Millbourne Mills Co.*, 22 A. B. R. 442, 172 Fed. 177 (C. C. A. Pa.).

4. *Fourth St. Nat'l B'k v. Millbourne Mills Co.*, 22 A. B. R. 442, 172 Fed. 177 (C. C. A. Pa.).

5. *Fourth St. Nat'l B'k v. Millbourne Mills Co.*, 22 A. B. R. 442, 172 Fed. 177 (C. C. A. Pa.); *In re McDonald*, 23 A. B. R. 51, 173 Fed. 99 (D. C. Mass.); *Crucible Steel Co. v. Holt*, 23

A. B. R. 302, 174 Fed. 127 (C. C. A. Ky.), quoted at § 1208. And the powers with which § 67 (a) and § 70 (e) vest the trustee are powers not given an assignee under the Act of 1867. *In re McDonald*, 23 A. B. R. 51, 173 Fed. 99 (D. C. Mass.).

6. *Fourth St. Nat'l B'k v. Millbourne Mills Co.*, 22 A. B. R. 442, 172 Fed. 177 (C. C. A. Pa.).

And in conjunction with clause (c) of § 67 which reads:

"That all conveyances, transfers, assignments or encumbrances of his property, or any part thereof, made or given by a person adjudged a bankrupt under the provisions of this act subsequent to the passage of this act and within four months prior to the filing of the petition, with the intent and purpose on his part to hinder, delay, or defraud his creditors, or any of them, shall be null and void as against the creditors of such debtor, except as to purchasers in good faith and for a present fair consideration; and all property of the debtor conveyed, transferred, assigned, or encumbered as aforesaid shall, if he be adjudged a bankrupt, and the same is not exempt from execution and liability for debts by the law of his domicile, be and remain a part of the assets and estate of the bankrupt and shall pass to his said trustee, whose duty it shall be to recover and reclaim the same by legal proceedings or otherwise for the benefit of the creditors." "And all conveyances, transfers, or incumbrances of his property made by a debtor at any time within four months prior to the filing of the petition against him, and while insolvent, which are held null and void as against the creditors of such debtor by the laws of the State, Territory, or District in which such property is situate, shall be deemed null and void under this Act against the creditors of such debtor if he be adjudged a bankrupt, and such property shall pass to the assignee and be by him reclaimed and recovered for the benefit of the creditors of the bankrupt."

And in conjunction with § 47 (a) (2) as amended in 1910, reading:

"And such trustee, as to all property in the custody, or coming into the custody, of the bankruptcy court shall be deemed vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon; and also, as to all property not in the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies and powers of a judgment creditor holding an execution duly returned unsatisfied."

And finally in conjunction with §§ 60 and 67 (c) and (f) of the Act relative to voidable preferences and nullified liens obtained by legal proceedings within the four months preceding the bankruptcy.

State Bk. v. Cox, 16 A. B. R. 36, 143 Fed. 91 (C. C. A. Ills.): "The formal title of the bankrupt to the estate passes to the trustee (70a) 'by operation of law' as of the date of adjudication, but the trustee is vested as well under subdivisions (4) and (5) with property transferred in fraud of creditors, and 'property which prior to the filing of the petition' the bankrupt 'could by any means have transferred' or which might have been levied upon and sold. Thus the narrow construction of the first-mentioned provision, which is sought for escape from liability for the plain violation of the Act through the seizure in question, not only ignores these succeeding and comprehensive clauses, but it would nullify the terms and entire policy of the act for the protection of creditors against spoliation of estates subject to bankruptcy proceedings."

Now, it is fundamental in law that a debtor cannot himself avoid his own fraudulent transfer, this being so because the fraudulent transfer gives a good title against him and no court will listen to his plea for declaring it null nor let him so stultify himself as to say he transferred the property fraudulently and now wants it back. So it is only creditors who

can avoid fraudulent transfers, although in a qualified sense the debtor still has the title.⁷

Andrews v. Mather, 9 A. B. R. 299, 134 Ala. 358: "Although property which has been fraudulently conveyed ceases to belong to the grantor, so far as any claim he himself can set up is concerned, yet the law regards property which has been fraudulently conveyed as still the property of the grantor, so far as creditors are concerned. The assignee in bankruptcy is an officer created for the benefit of creditors, and he is permitted to regard property fraudulently conveyed in the same way in which creditors are permitted to regard it."

Chesapeake Shoe Co. v. Seldner, 10 A. B. R. 466, 473, 122 Fed. 593 (C. C. A. Va.): "As between the bankrupt and his fraudulent grantee, the bankrupt has no title and to give any effect, or even meaning to Clause 4 (§ 70) we must construe the words 'title of the bankrupt' as between the bankrupt and his creditors."

Compare, inferentially, to same effect, *Bardes v. Bank*, 4 A. B. R. 175, 175 U. S. 526: "It was argued for the appellant that the clause cannot apply to a case like the present one, because the bankrupt could not have brought a suit to set aside a conveyance made by himself in fraud of his creditors. But the clause concerns the jurisdiction only, and not the merits, of a case; the forum in which a case may be tried, and not the way in which it must be decided; the right to decide the case, and not the principles which must govern the decision. The bankrupt himself could have brought a suit to recover property, which he claimed as his own, against one asserting an adverse title in it; and the incapacity of the bankrupt to set aside his own fraudulent conveyance is a matter affecting the merits of such an action, and not the jurisdiction of the court to entertain and determine it."

Likewise an unrecorded or defectively recorded mortgage or other voluntarily given lien upon the bankrupt's property is always good between the parties; so that, again, it is only as to creditors that unrecorded liens are void. So when the statute, in § 70 (a), says the trustee shall be vested with the title of the bankrupt, the provision must not be thought to limit the trustee's rights to the mere rights of the bankrupt.

As long as other sections of the Act give the trustee greater rights than merely those that might be asserted by the bankrupt, the statute must be construed to mean that he takes the bankrupt's title and rights and in addition thereto takes more—takes also the rights of creditors, not only those rights that have been already actually asserted by some creditor but any and all that might have been asserted had the trustee been a judgment creditor who had levied on the property in his custody or who holds an unsatisfied execution as to property not in his custody, as well as the rights of creditors under State law to avoid fraudulent transactions.

The Bankruptcy Act, itself, then, gives the trustee by § 70 (a) not only the bankrupt's own title, but also expressly vests in him, by § 70 (a) (4), title to all property transferred by the bankrupt in fraud of cred-

7. *Thomas v. Sugarman*, 19 A. B. R. 509, 157 Fed. 669 (C. C. A. N. Y.), quoted *supra*.

itors; and, by § 70 (c), gives him the right to clear away from the bankrupt's title to property all fraudulent transfers of such title which any creditor might, under State law, have avoided; and, by § 67 (a) and § 47 (a) (2) as amended in 1910, gives him the right to clear away from the bankrupt's title to property all liens that would for any reason not have been valid liens against the claims of creditors under State law had there been no bankruptcy, § 47 (a) (2) as amended in 1910,⁸ giving to the trustee in addition to the rights or remedies already asserted by any creditor, all rights and remedies which any creditor might have had had there been no bankruptcy and had such creditor levied execution or acquired a lien by equitable process or held an execution returned unsatisfied, all which rights are in addition to the peculiar rights conferred on the trustee by the special provisions of the Bankruptcy Act relative to avoiding preferential transfers and liens obtained by legal proceedings within the four months preceding the bankruptcy.

It is doubtless true that the trustee's title since the Amendment of 1910 is the most extensive and complete of any in jurisprudence.

It also must be borne in mind that the Amendment of 1910, by placing the trustee in the position of an execution creditor with a levy on the property in his custody and with an unsatisfied execution on the property not in his custody, gives him more than the rights which any creditor might have chanced already to have asserted. It gives him in addition thereto, all rights which would have been obtainable by creditors under State law had the trustee been an officer holding an execution or equitable process in behalf of all creditors. This right is not a right derived from existing creditors. It is not a transfer from any creditor by operation of law of that creditor's existing lien or levy, as seems to have been held in one case.⁹ It is a right derived from the statute itself conferring upon the trustee the attributes of a creditor "armed with process."

In *re Farmer's Co'op. Co.*, 30 A. B. R. 187, 190, 202 Fed. 1008 (D. C. N. D.): "In my judgment, however, § 47 of the Bankruptcy Act as amended does not depend upon any such distinction. The trustee in bankruptcy derives his rights and powers from the statute, and not from the creditors of the estate. If any creditor under local statute can obtain priority over an unfiled or unrecorded instrument, by levy of attachment or execution, the trustee in Bankruptcy, under § 47 as amended, has all the rights and remedies of such creditor. * * *

"A fair interpretation of the statute in the light of the weight of authority, as above pointed out, gives to the trustee all the rights of the most favored creditor under the local law and any property thus held by the trustee becomes a part of the general estate to be apportioned among all creditors in accordance with the provisions of the Bankruptcy Act on that subject."

8. This amendment ought to have been inserted at § 70 or § 67 rather than at § 47. It was placed at § 47 through one of those exigencies of leg-

islation which sometimes occur to mar the symmetry of statutory enactments.

9. In *re Flatland*, 28 A. B. R. 476, 196 Fed. 310 (C. C. A. Wash.).

§ 1139. General Discussion of Trustee's Title and Rights.—As noted later in § 1208, et seq., the underlying theory of the Act of 1898, as well as of all former acts of the United States and also of those of England, denied to the trustee in bankruptcy, except as to fraudulent transfers and holdings, any right which creditors merely *might* have exercised but had not already actually exercised, or placed themselves in position, under State law, to exercise, the idea being that the bankruptcy adjudication in no wise in and of itself affected the title, but merely transferred whatever rights the bankrupt or any of his creditors actually had acquired—save and except always, of course, as to fraudulent transactions and as to preferences and liens by legal proceedings within the four months period voidable by the peculiar provisions of Bankruptcy Law.

According, indeed, to some of the decisions before the Amendment of 1910, it was even doubtful whether, as to unrecorded liens, in States where void only as to creditors “armed with process,” the trustee succeeded to the rights of all creditors who were thus “armed with process”—this subrogation to such rights being confined, by some of the decisions, merely to the rights of those creditors who had acquired liens by legal proceedings within the four months preceding the bankruptcy, void as to the trustee under § 67f but preservable for the benefit of the estate upon order duly made; indeed, such would seem to have been the logical result of the holding that the trustee succeeded to the rights only of such creditors who had been armed with process, for certainly he did not succeed to the rights of any creditor armed with process as to any levy *not* made within the four months preceding the bankruptcy, but rather took title subject thereto. Thus the ultimate logic of the holdings of the courts before the Amendment of 1910, must eventually have narrowed the trustee's title as successor to the creditors' rights, to a short range.

The idea of bankruptcy jurisprudence during its entire history, up until the Amendment of 1910, was that the bankruptcy picked up the estate precisely where it found it, giving the trustee thereby no additional rights save such as were conferred by the peculiar provisions of the act relative to preferences and legal liens acquired within the four months period, although giving to him all rights possessed by the bankrupt at the time of the bankruptcy, and all rights then asserted by any creditor or which any creditor had already placed himself in a position to assert.¹⁰

[Before Amendment of 1910 to Bankr. Act, § 47 (a) (2).] Warehousing Co. (Security Warehousing Co.) *v.* Hand, 19 A. B. R. 291, 206 U. S. 415: “It is no new doctrine that the assignee or trustee in bankruptcy stands in the shoes of the bankrupt, and that the property in his hands, unless otherwise provided in the Bankrupt Act, is subject to all of the equities impressed upon it in the hands of the bankrupt. This has been the rule under former acts and is now the rule.

10. Trustee's title and rights under State Insolvency Law, *In re Little*—present law, before Amendment of field, 19 A. B. R. 18, 158 Fed. 838 (C. 1910, much as under Massachusetts C. A. Mass.).

Hewitt v. Berlin Mach. Works, 191 U. S. 296, 11 Am. B. R. 709, * * * Thompson v. Fairbanks, 496 U. S. 546, 526, 13 Am. B. R. 437, * * * Humphrey v. Tatman, 198 U. S. 91, 14 Am. B. R. 74. * * * York Mfg. Co. v. Cassell, 201 U. S. 344, 352, 15 Am. B. R. 633. * * * In the Hewitt case, there was a sale of property to the bankrupt upon condition that the title should not pass until the property was paid for. Such a conditional sale was good in New York State, where the contract was made, and it was held good as against the trustee in bankruptcy, because it was good against the bankrupt. It was further held that the property was not, under the facts and the law of New York, such as might have been levied upon and sold under judicial process against the bankrupt, nor could she have transferred it, within the meaning of § 70 of the Bankruptcy Act. It was a clear case for the application of the doctrine that the trustee stands in the shoes of the bankrupt, and there was nothing in the act which made any inconsistent provision. In Thompson v. Fairbanks, the question arose as to the validity of a chattel mortgage (which had been duly filed) upon after-acquired property as against the trustee in bankruptcy of the mortgagor. The mortgagee took possession of the mortgaged property before the filing of the petition in bankruptcy, and the question raised was whether there was a violation of any provision of the Bankruptcy Act. It was held that the validity of such a mortgage was a local, and not a Federal, question, and that in such case this court would follow the decisions of the State court; and as in Vermont such a mortgage was good, and the taking possession of the property related back to the date of the mortgage, even as against an assignee in insolvency, it was good as against the trustee in bankruptcy. It was said: 'Under the present Bankruptcy Act, the trustee takes the property of the bankrupt, in cases unaffected by fraud, in the same plight and condition that the bankrupt himself held it, and subject to all the equities impressed upon it in the hands of the bankrupt, except in cases where there has been a conveyance or encumbrance of the property which is void as against the trustee by some positive provision of the act.' As there was no provision therein making such a mortgage void, the mortgagee was permitted to enforce his mortgage as a valid instrument, and to retain possession of the property. There was no fraud in fact and no transfer of any property in fraud of creditors, and the property was not, at the time of the filing of the petition in bankruptcy, or at the time of the adjudication, liable to levy and sale under judicial process against the bankrupt. It had already been taken possession of by the mortgagee under a valid mortgage, and was not subject to any other liability of the mortgagor. Humphrey v. Tatman reiterates the principle that whether such a mortgage as is referred to in the Fairbanks case is good or bad depends upon the State law. In York Mfg. Co. v. Cassell, the same question arose as in the Hewitt case. There was a sale of property to one who thereafter became bankrupt, with a condition that no title to the property should pass until it was paid for. Such a conditional sale was good under the Ohio law, where the instrument was executed, except as to those creditors who, between the time of the execution of the instrument and the filing thereof, had obtained some specific lien upon the property. There were no such creditors, and hence there was no one who could question the validity of the instrument at the time the trustee's title would have accrued, unless it was the trustee in bankruptcy. He made the claim that the adjudication in bankruptcy was equivalent to a judgment or an attachment or other specific lien on the property, so as to prevent the vendor from asserting its title and its legal right to remove the property on account of the non-payment of the purchase price. We held that, as the conditional sale was valid by the law of Ohio, except as to a certain class of creditors, if there were no such creditors there was

no one who could question the validity of the instrument; that the adjudication in bankruptcy did not give the trustee the right to do so, because in that case the adjudication did not operate as the equivalent of a judgment or attachment or other specific lien on the property. The trustee represented no one who had that right as there were no creditors who had liens on the property when the title of the trustee to the property of the bankrupt accrued. Section 70 of the Bankrupt Act had no application. There was no property within either the fourth or fifth subdivision of that section. The fact that if there had been a creditor of the bankrupt of the class mentioned who had obtained a specific lien on the property prior to the adjudication in bankruptcy, the trustee could in that case have enforced the same, did not make any difference, because no such thing had been done when the adjudication in bankruptcy was made. This court had theretofore approved the remark *In re New York Economical Printing Co.*, 6 Am. B. R. 615, 49 C. C. A. 133, 110 Fed. 514, 518, that the present Bankrupt Act contemplates that a lien good as against the bankrupt and all of his creditors at the time of the filing of the petition in bankruptcy should remain undisturbed. *Hewitt case*, *supra*. Upon these facts it was reiterated that the trustee takes the property as the bankrupt held it. The case at bar bears no resemblance in its facts to the cases just cited. There was no valid disposition of the property in the case before us, or any valid lien. The so-called warehouse receipts issued by the warehousing company to the knitting company, upon the facts of this case, gave no lien under the law in Wisconsin, in which State they were issued. In such case this court follows the State court. *Etheridge v. Sperry*, 139 U. S. 266; *Dooley v. Pease*, 180 U. S. 126. By § 70a, the trustee in bankruptcy is vested, by operation of law, with the title of the bankrupt to all property transferred by him in fraud of his creditors, and to all property which, prior to the filing of the petition, might have been levied upon and sold by judicial process against him; and, by subdivision (e) of the same section, the trustee in bankruptcy may avoid any transfer by the bankrupt of his property which any creditor of the bankrupt might avoid, and may recover the property so transferred, or its value. Here are special provisions placing the title to the property transferred by fraud or otherwise, as mentioned, in the trustee in bankruptcy, and giving him the power to avoid the same. The title to this property was in the knitting company. There had been no valid pledge of it, because the possession had been, at all times, in the knitting company, and it could have been levied upon and sold under judicial process against the knitting company at the time of the adjudication in bankruptcy. The security company had, of course, full knowledge that the knitting company in fact, at least, shared in the possession of the property. It was itself an actor, or it acquiesced in the arrangement under which it had, at most, a partial, possession, and even that was subject to the control of the knitting company. The method taken to store the property was, as found by the District Court, a mere device or subterfuge to enable the bankrupt to hypothecate the receipts, and thus raise money upon secret liens on property in the possession of the pledgor and under its control; and such scheme, the court said, ought not to receive judicial sanction. Such a scheme, under the facts, and as carried out in this case, and with regard to Wisconsin law, was a fraud in fact, and neither the receipts nor the so-called pledge could be asserted against any of the creditors. It was held by the Circuit Court of Appeals in a case arising in Wisconsin, relative to a chattel mortgage, which gave power to the mortgagor to make sales from the mortgaged property for his own use and benefit, that such a mortgage was fraudulent in fact, so it could not be asserted even against general creditors; citing Wisconsin cases. *Re Antigo Screen Door Co.*, 10 Am. B. R. 306, 59 C. C. A. 248, 123 Fed. 249, 254. A further question was

ruled upon in the above-cited case. It was in respect to a second mortgage upon chattels, which had not been properly filed, but the mortgagee had taken possession of the mortgaged property prior to the filing of the petition in bankruptcy, although long subsequent to the giving of the mortgage, and it was held that the mortgagee might hold the property as against the trustee in bankruptcy representing general creditors. There was no fraud in fact alleged. It was said by Judge Jenkins, in delivering the opinion of the court: 'When the statute (Rev. Stat. Wis. 1898, § 2313) declares that a chattel mortgage shall be invalid against any other person than the parties thereto unless possession be delivered and retained, or the mortgage be filed,—there being no actual fraud and no collusive delay in the filing or the taking of possession,—we think the statute must be construed to mean that the omission to file or to take possession renders the mortgage invalid only as to the creditor who, by execution or attachment, has acquired a lien upon the property.' The case illustrates the distinction taken between fraud in fact and the mere failure to file a mortgage otherwise valid against the world. Under the circumstances of this case we are satisfied there was no valid pledge and no equitable lien in favor of the interveners which would take precedence of the title of the trustee by virtue of the special provisions of the Bankruptcy Act." The principles of this case are further explicated in *In re Standard Tel. & Elec. Co.* (*Knapp v. Milw. Tr. Co.*), 24 A. B. R. 761, 216 U. S. 545, quoted at §§ 1211, 1258.

In *re Bailey & Sons*, 21 A. B. R. 911, 166 Fed. 982 (D. C. Pa.): "The doctrine of *York Mfg. Co. v. Cassell*, 15 A. B. R. 633, 201 U. S. 344, that the trustee ordinarily takes no better title to the property than the bankrupt himself had, does not apply. It may be true that the present transaction was good between the claimant and the bankrupt, but under the facts in proof the trustee's title is better than the bankrupt's because the Bankruptcy Act declares the attempted transfer to be a voidable preference and expressly authorizes the trustee to avoid it."

Although, to be sure, the trustee was not confined to the bankrupt's title and rights, yet no force nor effect was given to the seizure or possession of the bankruptcy court itself, although such seizure was as effectually a sequestration as could possibly be a seizure by the legal or equitable process of any other court; whereby, also, creditors' hands were tied from asserting rights against the property, and yet the selfsame creditors were bound by the bankrupt's own title. The effect of such construction of the act was to make unrecorded liens, in States where "creditor" was construed to mean a creditor who had fastened a lien by levy of process upon the property, perfectly valid in the bankruptcy court, although a similar sequestration in the State court might have nullified such unrecorded liens. In this way the object of the recording statutes in the prevention of secret liens was oftentimes quite defeated in bankruptcy. Indeed, in many States general creditors came to find they had less rights in the bankruptcy court than in the State court, as to transfers or instruments voidable only as to creditors "armed with process." Such, indeed, was the effect of the noted case of *York Mfg. Co. v. Cassell*, in the State where the case arose.

Before the Amendment of 1910, the statute, in §§ 67 and 70, as well as

elsewhere, seemed to strive to give the trustee the same rights and remedies that any creditor "might" have exercised to avoid transfers, whether actually exercised or not, which provisions might naturally have been construed to give him either the right to take all necessary steps that would have been required of such creditor, or, perhaps, even to have dispensed with such preliminary steps altogether; and certainly, even before the Amendment of 1910, the pendency of the bankruptcy proceedings having tied the creditors' hands so that they could not help themselves with their ordinary remedies, it might have seemed not only natural, but also a correct construction of the law to have held that the trustee was subrogated not only to all rights and remedies for avoiding transfers which any creditor had already begun to assert, but also to all rights and remedies which any creditor "might" have asserted, as, indeed, the very wording of § 70 (e) would seem to have indicated.

However, the courts rejected such construction, as inapplicable except in cases of actual fraud and where State law did not require "arming with process;" and they relegated the trustee to the "shoes of the bankrupt," where he remained until the Amendment of 1910, which lifted him, out of the shoes of the bankrupt and placed him in the position of a creditor "armed with process."

It is manifest that this amendment changes materially the title of the trustee, so that the rules enunciated in the decisions prior to the Amendment of 1910 must be further qualified by the proviso that the trustee is limited by the bankrupt's title, only in so far as a creditor under the State law would have been bound thereby had such creditor possessed a levy upon the property at the time of its coming into the custody of the bankruptcy court, or had had an execution returned unsatisfied as to the property not in the custody of the bankruptcy court.¹¹

In *re Franklin Lumber Co.*, 26 A. B. R. 37, 187 Fed. 281 (D. C. Pa.): "It is to be noted that § 47a (2) as amended by the Act of June 25th, 1910 applies to the present dispute. Under that amendment, if properly coming into the custody of the court be claimed by another, the trustee is vested with all the rights, remedies, and powers of a creditor holding a lien by legal or equitable proceedings thereon. An agreement therefore which would previously have been valid between the parties—such, for example, as was considered in *Davis v. Crompton* (C. C. A. 3d Cir.) 20 A. B. R. 53, 158 Fed. 735 (209 U. S. 548)—is no longer necessarily valid against the trustee. He is in the position of a creditor holding a legal or equitable lien, and the agreement is to be scrutinized from that point of view. * * * Assuming that the bankrupt would be bound by the words of this agreement and could not deny it to be a lease, his trustee is not so bound, and may contend that the contract is really one of conditional sale. In such a contention he may offer any competent and relevant evidence, and it is obvious I think that the conduct of the parties may ordinarily throw much light on the true meaning of their agreement. If they treat

11. See § 1270 et seq., for detailed discussion of trustee's rights by the Amendment of 1910.

it as a contract of sale, it makes no difference what name they have given it. * * * In reality it has always been a contract of conditional sale, although it may be true that the bankrupt himself would not have been permitted to prove its true character. Neither could the trustee have proved its true character until the Act of June 25, 1910, was passed, but since that date he has been put upon the footing of a creditor with a legal or equitable lien, and may take full advantage of such rights. Whenever therefore such a creditor may attack a contract, in form a bailment, on the ground that it is really a conditional sale, and may support the attack by competent and relevant evidence that throws light on the true meaning of the contract—the trustee has the same right. The mere form of the agreement does not bind him, as it might bind the bankrupt."

To the extent, and only to the extent, then, that a creditor, were he a levying creditor on the property in the custody of the court, or a creditor holding an unsatisfied execution as to property not in the custody respectively, would be bound, the trustee is bound and limited by the bankrupt's rights and by the rights already possessed or asserted by creditors.

The complete statement, then, of the trustee's title and rights, since the Amendment of 1910, is that above given at § 1137.

Hereafter, beginning at § 1143, we will take up in detail the various leading propositions and their subdivisions, fully explicating the rights, title and remedies of the trustee in bankruptcy.

§ 1140. Local Law Determines Effectiveness of Transaction to Accomplish Transfer of Title, Also Time Title Passes.—In all the several branches of the discussion of the trustee's title and rights, whether they be those derived as the successor of the bankrupt or of the creditors, or be those independently conferred by the special provisions of the bankruptcy act itself, it is to be borne constantly in mind that the state law determines the efficiency of acts and transactions to effect the transfer of title of the property involved and also the time of the passing of title.¹²

Inferentially and suggestively *In re Baxter & Co.*, 18 A. B. R. 450, 154 Fed. 22 (C. C. A. N. Y.): "All rules concerning the transfer of property are 'primarily at least, a matter of State regulation, and not one of purely commercial law' (*Etheridge v. Sperry*, 139 U. S. 276) and State laws, creating interests in or liens upon property without the State, control the federal courts whenever the question arises as to the validity, extent and all the conditions of such an interest or lien. Thus, the effect and validity of chattel mortgages and general assignments are determined by the law of the State in which they are made."

And the reason of the rule is obvious. The Bankrupt Act did not—before the Amendment of 1910—seek to give creditors through the trustee in bankruptcy any greater rights in each State than they would have had without the law, except where it conferred upon the trustee the

¹². In *re Doran* (*Moorman v. Beard*), 18 A. B. R. 760, 154 Fed. 467 (C. C. A. Ky.). Compare, instance, *In re Reynolds*, 18 A. B. R. 666, 153 Fed. 295 (D. C. Ark.); impliedly, *Goodwin v. Murchison Nat. Bank*, 22 A. B. R. 703, 145 N. Car. 320.

peculiar rights granted by its special provisions relative to preferences, legal liens and fraudulent conveyances.

In *re Cohn*, 22 A. B. R. 761, 171 Fed. 568 (D. C. N. Dak.): "The cardinal principle of the Bankruptcy Act is to grant to creditors only those rights which would have been theirs had bankruptcy not supervened."

And by the Amendment of 1910 it simply gave to the bankruptcy proceedings the effect of arming the trustee with process, so that the creditors might not be debarred by the bankruptcy from asserting in behalf of all creditors the rights given to creditors by State law dependent on their being "armed with process."

The essential nature of the transfer or seizure, as to its effectiveness in each case to transfer title is, in pursuance of the same theory, left to the rules of property of the State, so that it is possible, even with regard to the peculiar rights conferred by the Act relative to preferences, legal liens and fraudulent conveyances within four months, that what will amount to a voidable bankruptcy preference in one State will not amount to a voidable bankruptcy preference in another State, and that what will amount to a void lien by legal proceedings in one State will not amount to a void lien in another State, the power of the particular transaction in each instance to effect a transfer of title, and, incidentally, the time such transfer of title shall be considered as having taken place and the kinds of property affected thereby, being left to the rules of each State.

Thus, it is quite possible, in accordance with the rules that precisely the same facts might lead to different results in different States, depending in great degree—even in regard to the peculiar titles conferred by the Bankruptcy Act itself as aforesaid—upon the effectiveness of those facts to transfer title in the several instances.

In other words, the nature of the transaction, that is to say, whether for instance, it amounts to a sale or bailment or pledge or mortgage or some other transfer of property, or whether sufficient delivery has been made to pass title, or whether recording or filing of an instrument be required and, if so, as to whom it will be void for lack of recording, etc., etc., is to be determined by State law, and the bankruptcy court will take it as so determined.¹³

13. In *re Waite-Robbins Motor Co.*, 27 A. B. R. 541, 192 Fed. 47 (D. C. Mass.); *Rosenbluth v. DeForest, etc., Co.*, 27 A. B. R. 359 (Sup. Ct. Conn.); *Title Guar. & Surety Co. v. Witmire*, 28 A. B. R. 235, 195 Fed. 41 (C. C. A. Mich.), decided under the law of Minnesota. Thus, as to bailment, In *re Morris*, 19 A. B. R. 422, 156 Fed. 597 (D. C. Pa.), quoted at § 1228.

Thus, it has been held, in accordance

with local law, that an equitable assignment of a debt, not requiring to be recorded, takes effect as consummated at the time of giving notice to the debtor. In *re Wilson*, 23 A. B. R. 814 (D. C. Hawaii).

So, the local law will govern as to what constitutes a legal or equitable assignment. In *re Stiger*, 29 A. B. R. 253, 202 Fed. 791 (D. C. N. J.).

In *re Hartlagen*, 26 A. B. R. 532, 189 Fed. 546 (D. C. Pa.): "The interpretation of the contract is for the court and the intention of the parties must be ascertained from the writing. In bankruptcy its construction and validity must be determined by the local laws of the state." (This case further quoted at § 1242.)

However, after the State law has once settled the nature of the transaction, once determined whether the facts are sufficient to constitute a transfer of title, and, if so, the time the transfer takes effect and the property affected thereby, then the Bankrupt Act may forthwith step in and declare whether it is a voidable preference or a nullified legal lien.

§ 1141. Also Governs Validity, Except Where Peculiar Rights as to Preferences, Liens by Legal Proceedings, etc., Conferred by Act Itself, Involved.—Where not affected by the peculiar provisions of the Bankruptcy Act, the law of the State will control in bankruptcy as to the validity of mortgages and other liens, and as to ownership and other interests in property.¹⁴

14. Compare similar proposition as to marshalling of liens, etc., post, § 1896. Compare similar rule as to allowability of claims, ante, § 780. *Dodge v. Norlin*, 13 A. B. R. 176, 133 Fed. 363 (C. C. A. Colo.); *Young v. Upson*, 8 A. B. R. 377, 115 Fed. 192 (D. C. N. Y.): Statute making presumptively fraudulent, assignments of "goods and chattels" not accompanied with delivery, does not apply to assignments of book accounts as collateral.

In *re Tice*, 15 A. B. R. 97, 139 Fed. 58 (D. C. Pa.); In *re Beede*, 14 A. B. R. 697, 138 Fed. 441 (D. C. N. Y.); In *re Gosch*, 9 A. B. R. 613 (D. C. Ga.), reversed, on other grounds, in 12 A. B. R. 149, 126 Fed. 627 (C. C. A. Ga.); In *re Sheets Ptg. & Mfg. Co.*, 14 A. B. R. 668 (D. C. Ohio); In *re Dry Dock Co.*, 16 A. B. R. 328 (C. C. A. N. Y.).

In *re Thackara Mfg. Co.*, 15 A. B. R. 258, 140 Fed. 126 (D. C. Pa.), where the lien of an execution levy was held in accordance with state law to be vitiated by use as security to compel payments by judgment debtor, rather than as satisfaction by sale and application of proceeds. *Morgan v. Nat'l Bk.*, 16 A. B. R. 644, 145 Fed. 466 (C. C. A. W. Va.). Also, in *re McArdle*, 11 A. B. R. 358, 126 Fed. 442 (D. C. Mass.); where it was held, that the mortgagee of the bankrupt's liquor license was not entitled to the proceeds of the sale of the liquor license sold by the trustee; since the police authorities refused to recognize the right to mortgage the license.

In *re McKay*, 16 A. B. R. 238 (D. C.

N. Y.), as to whether income of a spendthrift trust passes to the trustee.

In *re Noel*, 14 A. B. R. 725, 137 Fed. 694 (D. C. Md.), wherein it was held that a State statute requiring mortgages to be recorded within six months of their execution can not be evaded by making new mortgages every six months as renewals and keeping them all off the records, although none are more than six months old until replaced and although the last one is recorded within six months of its execution and before bankruptcy. Also, *Deland v. Miller*, 11 A. B. R. 744, 119 Iowa 368; In *re Josephson*, 8 A. B. R. 423 (D. C. Ga.), as to recording; In *re Kellogg*, 7 A. B. R. 623, 113 Fed. 120 (D. C. N. Y., affirming 6 A. B. R. 389); In *re Rogers & Woodward*, 13 A. B. R. 82, 132 Fed. 560 (D. C. Vt.); In *re Smith & Shuck*, 13 A. B. R. 105, 132 Fed. 301 (D. C. Iowa); In *re Mullen*, 4 A. B. R. 224, 101 Fed. 413 (D. C. Mass.); impliedly, *Allen v. Hollander*, 11 A. B. R. 756, 128 Fed. 159 (C. C. A. Mass.).

In *re Greene*, 13 A. B. R. 507, 134 Fed. 137 (D. C. Conn.): In this case it was held, that the formalities as to recording, etc., are to be determined by the law of the State where the property is located and not by that of the residence of the parties.

In *re Standard Tel. Co.*, 19 A. B. R. 491, 157 Fed. 106 (D. C. Wis., affirmed sub nom. *Knapp v. Milw. Tr. Co.*, 20 A. B. R. 671, 162 Fed. 675 C. C. A.), quoted post, this same section affirmed sub nom. In *re Standard Tel. & Elec. Co.*, 24 A. B. R. 761, 216 U. S. 545; In

In considering the following quotations in this section, as also the citations in the notes, care must be taken to distinguish between the cases cited or quoted as to whether they arose before or after the Amendment of 1910 to Bankruptcy Act, § 47 A (2), whereby the trustee was lifted out of his former station "in the bankrupt's shoes" and was given the standing of a "creditor armed with process;" for, whilst it is still true that the local law governs the validity of liens, contracts and other transactions in bankruptcy (except where the peculiar rights conferred by the bankruptcy law as to preferences and liens by legal proceedings within four months are concerned) yet it is no longer so because the trustee "stands in the bankrupt's shoes," which was apparently the basis of most of the decisions, since he now stands also in all respects as a creditor and is bound by the bankrupt's title and rights only in so far as a creditor would be so bound. Thus, it is the State law that governs.

Thompson v. Fairbanks, 13 A. B. R. 442, 196 U. S. 516: "The Supreme Court of the United States, in determining the validity of a chattel mortgage covering after-acquired property, will accept as decisive the settled law of the State in which the mortgage was given, as established by the decisions of its highest Courts."

Hiscock v. Varick Bk., 18 A. B. R. 6, 206 U. S. 28: "The contracts of pledge were made, executed and to be performed in the State of New York, and the rights of the parties were governed by the law of that State. No preference under the Bankruptcy Act was alleged or proved, nor was there any allegation or proof that the pledge of the securities was in fraud of the rights of the creditors or trustee. The questions of the extent and validity of the pledge were local questions, and the decisions of the courts of New York are to be followed by this court."

Hewitt v. Berlin Machine Wks., 11 A. B. R. 709, 194 U. S. 296: "And the circuit court of appeals, adhering to that decision, held, in this case, that, inasmuch as by the New York statute, a conditional sale such as that in question was void only as against subsequent purchasers or pledgees or mortgagees in good faith, the district court was right and affirmed the judgment. We concur in this view."

In re Galt, 13 A. B. R. 579, 120 Fed. 443 (C. C. A. Ills.): "The law of the

re *Agnew*, 25 A. B. R. 360 (D. C. Miss.); *Mattley v. Wolfe*, 23 A. B. R. 673, 175 Fed. 619 (D. C. Neb.); reversed in *Mattley v. Giesler*, 26 A. B. R. 116, 187 Fed. 970 (C. C. A. Neb.); *In re New England Breeders' Club*, 23 A. B. R. 689, 175 Fed. 501 (D. C. N. H.), a lien for materials and supplies; *In re Standard Tel. & Elec. Co.* (Knapp v. Milw. Tr. Co.), 24 A. B. R. 761, 216 U. S. 545; *In re Wade*, 26 A. B. R. 169, 185 Fed. 664 (D. C. Mo.); impliedly (Security) Warehousing Co. v. Hand, 19 A. B. R. 291, 206 U. S. 415, quoted at § 1137; *In re Pierce*, 19 A. B. R. 662, 157 Fed. 755 (C. C. A. N. Dak.); *Humphrey v. Tatman*, 14 A. B. R. 74, 198 U. S. 91; *York Mfg. Co. v. Cassell*,

15 A. B. R. 633, 201 U. S. 344; *Thomas v. Woods*, 23 A. B. R. 132, 173 Fed. 585 (C. C. A. Kans.); *Godwin v. Murchison Nat. Bank*, 22 A. B. R. 703, 145 N. Car. 320; *Smith & Bro. Typew. Co. v. Alleman*, 28 A. B. R. 699, 199 Fed. 1 (D. C. Pa.); [Perhaps, because of local law] *In re Flatland*, 28 A. B. R. 476, 196 Fed. 310 (C. C. A. Wash.); *In re Schoenfield*, 27 A. B. R. 64, 190 Fed. 53 (D. C. W. Va.); *Rode & Horn v. Phipps*, 27 A. B. R. 827, 195 Fed. 414 (C. C. A. Tenn.); *In re Geiver*, 28 A. B. R. 413, 193 Fed. 128 (D. C. S. Dak.); *In re East End Mantel & Tile Co.*, 29 A. B. R. 793, 202 Fed. 275 (D. C. Pa.).

State of Illinois with respect to conditional sales, as expounded by its Supreme Court, runs counter to the great weight of authority, but has become a rule of property in that State, and we are bound to observe it."

In *re Shirley*, 7 A. B. R. 303, 112 Fed. 301 (C. C. A. Ohio): "The law of Ohio is controlling upon the Federal court in questions arising upon the validity of chattel mortgages given and filed in that State upon property therein."

Bryant v. Swofford Bros. Co., 22 A. B. R. 111, 214 U. S. 279: "There is nothing in the nature of this contract which would forbid the parties from entering into it if it is valid by the laws of the State where made, but in bankruptcy the construction, and validity of such a contract must be determined by the local laws of the State, * * * That such a contract is a conditional sale and is valid without record is the law of Arkansas. *Triplett v. Monsur & T. Imple. Co.*, 68 Ark. 230. The trustee has no higher rights in this regard than the bankrupt."

In *re Antigone Screen Door Co.*, 10 A. B. R. 359, 123 Fed. 249 (C. C. A. Wis.): "We must accept as decisive the settled law of the State in which these chattel mortgages were given with respect to their validity."

In *re First Nat'l Bk. of Canton*, 14 A. B. R. 180, 135 Fed. 62 (C. C. A. Ohio): "In determining the validity of a chattel mortgage, this court will endeavor to follow the settled law of the State in which the transaction occurred."

In *re Butterwick*, 12 A. B. R. 536, 131 Fed. 371 (D. C. Pa.): "The trustee does not stand simply in the shoes of the bankrupt but is invested with the rights of his execution creditors. * * * This is to be determined by the local law."

In *re Heckathorn*, 16 A. B. R. 467, 144 Fed. 499 (D. C. Pa.): "This is a Pennsylvania transaction and is governed by local law. * * * The trustee in any such controversy is invested with the rights of creditors. * * * He is not limited, like an assignee under the State law, who is merely a representative of the debtor."

In *re Car & Loco. Wks.*, 14 A. B. R. 333 (D. C. Ills.): "Whether the petitioner is entitled to delivery of the locomotives is one of Illinois law, the place where the work was to be done and the delivery made."

In *re Worth*, 12 A. B. R. 566, 130 Fed. 927 (D. C. Iowa): "The notes of the receiver, being Iowa contracts, and payable in Iowa, are to be governed by the laws of that State relating to usury."

In *re Rodgers*, 11 A. B. R. 90, 125 Fed. 169 (C. C. A. Ills., reversed, on other grounds, sub. nom. *Bank v. Title & Trust Co.*, 14 A. B. R. 102, 198 U. S. 280): "Although the rule is otherwise in other States with respect to conditional sales we are in duty bound to defer to the law of the State in respect of property within that State."

In *re Miller & Brown*, 14 A. B. R. 439, 135 Fed. 868 (D. C. Pa.): "In cases of this character, the local law governs, the title of the trustee being determined by the question whether the arrangement with regard to the property is good as against creditors. If it is, the property may be reclaimed; but if not, it cannot be."

Zartman v. Nat'l Bk., 16 A. B. R. 152, 159, 106 App. Div. 406: "If the law in this State coincided with that of the State of Vermont the authority (*Thompson v. Fairbanks*, supra) would be decisive, but as we have concluded otherwise the case is not applicable."

In *re Cunningham v. Germ. Ins. Bk.*, 4 A. B. R. 367 (C. C. A. Ky.): "And the Court of Appeals of Kentucky, whose decisions in reference to the construction of the statutes of the State in relation to incorporations and the scope of the powers derived therefrom, we are required to follow, has recognized and adopted these propositions as applicable to the corporations of that State."

Davis v. Crompton, 20 A. B. R. 53, 158 Fed. 755 (C. C. A. Pa.): "The precise

extent to which such a conditional sale as we have in the present case, must be held invalid as to creditors, whether general or subsequent, and as to bona fide purchasers, mortgagees and pledgees, without notice, must depend upon the law of the State in which delivery of possession under the conditional sale has been made."

In *re Hickerson*, 20 A. B. R. 682, 162 Fed. 345 (D. C. Idaho): "The validity of such a mortgage [mortgage withheld from record by agreement] is a local question, and the decisions of the State courts will control."

In *re Chantler Suit & Cloak Co.*, 18 A. B. R. 498, 151 Fed. 952 (D. C. R. I.): "The latter case [*Thompson v. Fairbanks*, *supra*] also decides that, on the question of the validity of a mortgage upon after-acquired property, the federal court will follow the decisions of the State court."

In *re Burke*, 22 A. B. R. 69, 168 Fed. 994 (D. C. Ga.): "In the construction of State statutes defining property rights, the United States courts generally follow the rulings of the supreme appellate tribunal of the State. * * * This is peculiarly true as to real property, but it is also true as to other property rights. A clear statement of this doctrine may be found in *Bates' Federal Equity Procedure*, vol. 1, par. 9. The doctrine is particularly valuable in the administration of the bankruptcy law, for the reason that it conserves the liens which are created and recognized by the laws of the States. Statutes creating such liens, however, are in derogation of the rights of the general creditors, which are common rights, and under the well-known general principle such statutes must be strictly construed. Presumptively the possession of property by the bankrupt is vested by operation of law in the trustee, and when a claimant thereto insists upon a latent or undisclosed title he must bear the burden of showing his superior right or privilege. It is then the duty of the court to regard critically the statutes of the State, as authoritatively construed by State courts, and determine each case accordingly."

In *re Elletson Co.*, 23 A. B. R. 530, 174 Fed. 859 (D. C. W. Va.): "The Supreme Court has also determined that the question of whether such a deed of trust is valid or not is a local one and must be governed by the State court decisions which the Federal courts will follow."

In *re Gilligan*, 23 A. B. R. 668, 152 Fed. 605 (C. C. A. Ind.): "There being no creditors having special equities in the bankrupt estate, the sole question presented by this record is, whether, under the Indiana law, the conditional sale of personal property by a manufacturer to a retailer, for the purposes of resale, with an agreement to reserve title in the original vendor until paid for, is valid or not; and to determine such question we go to the Indiana law, in force at the time that the order appealed from was entered, as interpreted by her own courts." This case quoted further at § 1263.

Guarantee Title & Trust Co. v. First Nat. Bank, 24 A. B. R. 330, 185 Fed. 373 (C. C. A. Pa.): "Whether a conditional contract of sale, chattel mortgage or pledge of personal property is valid against the general creditors of the vendor, mortgagor or pledgor, or his trustee in bankruptcy, must be determined by the local laws of the State in which the transaction is had."

As decided by the highest court of the State.¹⁵

15. *Thompson v. Fairbanks*, 13 A. B. R. 437, 196 U. S. 516; In *re Galt*, 13 A. B. R. 579, 120 Fed. 64 (C. C. A. Ills.); In *re Rogers & Woodward*, 13 A. B. R. 82, 83, 132 Fed. 560 (D. C. Vt.); *Dodge v. Nordin*, 13 A. B. R. 176, 133 Fed. 363 (C. C. A. Colo.); *Dolle v. Cas-*

sell, 14 A. B. R. 52, 135 Fed. 52 (C. C. A. Ohio, reversed, on other grounds, in *York Mfg. Co. v. Cassell*, 15 A. B. R. 633, 201 U. S. 344); inferentially, In *re New England Breeders' Club*, 23 A. B. R. 689, 175 Fed. 501 (D. C. N. H.).

In re Andrae Co., 9 A. B. R. 135, 117 Fed. Rep. 561 (D. C. Wis.): "The law of a State as interpreted by its highest court governs the validity of the lien of chattel mortgages executed therein, if it does not fall within the preferences inhibited by the Bankruptcy Act."

In re Josephson, 8 A. B. R. 423, 116 Fed. 404 (D. C. Ga.): "As to a chattel mortgage not recorded, the State law not requiring recording and the mortgage not being withheld from record by agreement not given to hinder, delay nor defraud creditors."

In re Worth, 12 A. B. R. 572, 130 Fed. 927 (D. C. Iowa): "The construction of the local statute by the highest court of the State is, under the familiar rule, controlling upon the federal courts of that State."

In re Standard Tel. Co., 19 A. B. R. 491, 157 Fed. 106 (D. C. Wis., affirmed sub. nom. Knapp v. Milw. Tr. Co., 20 A. B. R. 671, 162 Fed. 675 C. C. A.) affirmed sub. nom. In re Standard Co., 24 A. B. R. 761, 216 U. S. 545: "The question of law arising in this case involves the construction of a Wisconsin statute. It is therefore a local question, as the Federal court in such a case adopts the ruling of the highest judicial tribunal of the State. This proposition is so familiar as to require the citation of no authorities."

In re Burke, 22 A. B. R. 69, 168 Fed. 994 (D. C. Ga.): "In the construction of State statutes defining property rights, the United States courts generally follow the rulings of the supreme appellate tribunal of the State."

Contra, In re Hull, 8 A. B. R. 302, 115 Fed. 858 (D. C. Vt.): "The decision of the Supreme Court of the United States that a chattel mortgage under which the mortgagor has the right to sell and replace goods to be included in the mortgage is fraudulent as matter of law and void as to other creditors, must be followed by the bankruptcy court although the highest State court had determined that such a mortgage is good and valid." But see editor's note to In re Hull and compare the later case of In re Rodgers & Woodward, 13 A. B. R. 82, 132 Fed. 560 (D. C. Vt.).

Or as decided by the highest court of the State which has passed upon the particular point, provided the same be not inconsistent with decisions of the highest court of the State.¹⁶

Or as interpreted by the higher federal courts in previous decisions.¹⁷

And it is held in other cases that where the question depends upon a rule of distribution in equity or of preference among various claimants to funds in the hands of the court for distribution in accordance with equitable principles, the Federal decisions control, and not those of the State where the contract was made.¹⁸

Likewise the Federal Courts, administering the general law of equity, as accepted in England, and as generally accepted in this country, may recognize and establish an equitable claim within the purview of the general rules of equity, though, under the decisions of the State Court, it has no status under the local law.¹⁹

16. In re Gilligan (Troy Wagon Works v. Hancock), 23 A. B. R. 668, 152 Fed. 605 (C. C. A. Ind.).

17. Instance, In re Burnham, 15 A. B. R. 549, 140 Fed. 926 (D. C. N. Y.).

18. Plow Co. v. McDavid, 14 A. B. R. 653, 137 Fed. 190 (C. C. A. Mo.).

19. James v. Gray, 12 A. B. R. 573, 131 Fed. 401 (C. C. A. Mass.). Compare, Hanson v. Blake, 19 A. B. R. 325, 150 Fed. 342 (D. C. Me.).

But where there is no authoritative rule on the subject in the State law then the general rules of law will apply.²⁰

In re Peasley, 14 A. B. R. 496, 137 Fed. 190 (D. C. N. H.): "Federal courts administer the general law of equity with respect to a subject upon which there is no positive or express rule of local law."

And where common law and not statutory law is involved, the Federal courts are not bound to follow the State decisions.²¹

And it is the law of the place where the performance of a contract is stipulated to be carried out that governs, not that of the place of its making.²²

Thus the local law governs as to recording;²³ and other formalities such as those required by statute as to sales of merchandise in bulk.²⁴

Also, local law governs as to pleading the statute of limitations as to fraudulent real estate transfers;²⁵ likewise, as to part performance taking a transaction out of the statute of frauds;²⁶ likewise, as to chattel mortgages covering after-acquired property, the State law determining when the lien is to be considered as attaching, whether at the date of the chattel mortgage or of the acquisition of the property;²⁷ likewise, also, as to who are meant by the term "creditors" when applied to unrecorded liens under State statute;²⁸ likewise, as to the effect of withholding mortgages from record;²⁹ and as to the validity of powers of sale in chattel mortgages.³⁰

20. Compare, analogously, to same effect, and even more extreme, recognizing claims as provable under general equity rules where under local law they had no status, *James v. Gray*, 12 A. B. R. 573, 131 Fed. 401 (C. C. A. Mass.).

21. In re Hess, 14 A. B. R. 635, 138 Fed. 954 (Ref. Pa.).

22. *Union Trust Co. v. Bulkeley*, 18 A. B. R. 43 (C. C. A. Mich.).

23. In re Nucklos, 29 A. B. R. 867, 201 Fed. 437 (D. C. Tenn.); Instance, In re Greene, 13 A. B. R. 504, 134 Fed. 137 (D. C. Conn.); In re Josephson, 8 A. B. R. 423, 116 Fed. 404 (D. C. Ga.).

Instance, In re Rogers & Woodward, 13 A. B. R. 82, 132 Fed. 560 (D. C. Vt.): Instrument sufficiently executed and recorded for chattel mortgage but insufficiently for real estate mortgage does not fix lien on lessee's buildings removable from premises where State law holds leaseholds to be real estate.

Instance, In re Gosch, 12 A. B. R. 149, 126 Fed. 627 (C. C. A. Ga., reversing 9 A. B. R. 610): Recording of conditional sale contract within 30 days of its "date," under State statute, "date" being construed to be date of delivery of the property, not of the contract.

Mottley v. Wolfe, 23 A. B. R. 673, 175 Fed. 619 (D. C. Neb.), reversed sub nom. *Mattley v. Giesler*, 26 A. B. R. 116, 187 Fed. 970 (C. C. A. Neb.).

24. *Wright v. Hart*, 14 A. B. R. 565 (N. Y. Ct. App., reversing 13 A. B. R. 491).

25. In re Dunavant, 3 A. B. R. 41, 96 Fed. 542 (D. C. N. C.).

26. In re Little River Lumber Co., 1 A. B. R. 482, 92 Fed. 585 (D. C. Ark., affirmed in 4 A. B. R. 313). Instance, conditional sales void in Pennsylvania: In re Butterwick, 12 A. B. R. 536, 131 Fed. 371 (D. C. Pa.).

27. *Thompson v. Fairbanks*, 13 A. B. R. 437, 196 U. S. 516; In re Chantler Cloak & Suit Co. 18 A. B. R. 498, 151 Fed. 952 (D. C. R. I.), quoted supra.

28. See post, § 1209.

29. See post, § 1222.

30. See post, § 1258.

Other Instances of State Laws Governing.—"Deed to Secure Debt" or "Chattel Mortgage," under Georgia law, In re Caldwell, 24 A. B. R. 495, 178 Fed. 377 (D. C. Ga.).

Attorney's fees in mortgage foreclosure. In re Torchia, 26 A. B. R. 188, 185 Fed. 576 (D. C. La.).

In re Grainger, 20 A. B. R. 166, 160

Local law governs as to the nature and validity of conditional sale contracts.³¹

Local law governs as to the validity of chattel mortgages withheld from record for a time but eventually recorded before bankruptcy.

In *re Wade*, 26 A. B. R. 169, 185 Fed. 664 (D. C. Mo.): "Whether and to what extent, a mortgage of this kind is valid is a local question, and the decisions of the State court will be followed by this court in such cases."

Local law governs as to the nature of the respective interests of vendors and vendees under land contracts.^{31a}

Likewise as to the effect of merely the bankruptcy proceedings as *lis pendens* against a creditor of a fraudulent grantee, levying attachment

Fed. 69 (C. C. A. Calif.), chattel mortgage on property not enumerated in statute as being capable of being mortgaged as against creditors, though good between the parties, is good against the trustee.

In *re Jacobs*, 1 A. B. R. 518 (D. C. La.): Louisiana Civil Code throwing burden of bona fides and valuable consideration upon mortgagee obtaining mortgage within three months of the mortgagor's failure.

In *re McBride & Co.*, 12 A. B. R. 81, 132 Fed. 285 (Ref. N. Y.): "Accord and Satisfaction" upon disputed royalties decided in accordance with New York Law.

In *re Kellogg*, 7 A. B. R. 623 (D. C. N. Y., affirming 6 A. B. R. 389): Mortgage on real estate in New York is merely a chose in action, giving the mortgagee no legal estate in the land but merely a lien thereon as security for his debt.

Gove v. Morton Trust Co., 12 A. B. R. 297 (Sup. Ct. App. Div. N. Y.): Chattel mortgage not filed when made but filed within four months preceding bankruptcy of mortgagor and made in pursuance of prior agreement made at time money loaned, held void in New York. If any judgment creditor existed, although no levy had been made before bankruptcy.

Skillen v. Endelman, 11 A. B. R. 766, 39 Misc. 261, 79 N. Y. Supp. 413: Chattel mortgage statute requiring either immediate change of possession or immediate filing.

In *re Goldman*, 4 A. B. R. 100, 102 Fed. 122 (D. C. N. Y.): Expiration of bankrupt's right to redeem lands sold under execution cuts off the trustee's right of redemption in New York.

Young v. Upson, 8 A. B. R. 377 (D. C. N. Y.): Chose in Action (book accounts here) not within N. Y. Statute requiring assignments of "goods and

chattels" to be accompanied with actual delivery.

In *re Austin*, 13 A. B. R. 136 (D. C. Hawaii): No attorney's lien on proceeds of judgment in Hawaii.

Blumberg v. Bryan, 6 A. B. R. 20, 107 Fed. 673 (C. C. A. Ala.): Wife may be adverse claimant in Alabama.

Hawk v. Hawk, 4 A. B. R. 463, 102 Fed. 679 (D. C. Ark.): Under State statute giving to wife, on divorce, one-third of husband's personalty, she has no interest in bankrupt estate if she has not obtained a divorce and may not have its distribution enjoined until she can obtain a divorce.

31. *Obiter, Guarantee Title, etc., Co. v. First Nat. Bank*, 24 A. B. R. 330, 185 Fed. 373 (C. C. A. Pa.), quoted *supra*; *Arctic, etc., Co. v. Armstrong Trust Co.*, 27 A. B. R. 562, 192 Fed. 114 (C. C. A. Pa.); *Nauman Co. v. Bradshaw*, 27 A. B. R. 565, 193 Fed. 350 (C. C. A. Ia.); In *re Hartdagen*, 26 A. B. R. 532, 189 Fed. 546 (D. C. Pa.); In *re Gilligan* (*Troy Wagon Wks. Co. v. Hancock*), 23 A. B. R. 668, 152 Fed. 605 (C. C. A. Ind.), quoted *supra*; In *re Gehris-Herbine Co.*, 26 A. B. R. 470, 188 Fed. 502 (D. C. Pa.); In *re Nelson*, 27 A. B. R. 272, 179 Fed. 203 (D. C. S. D.); *Mishawaka Woolen Mfg. Co. v. Westveer*, 27 A. B. R. 345, 191 Fed. 465 (C. C. A. Mich.); In *re Faulkner*, 25 A. B. R. 416, 181 Fed. 981 (D. C. Conn.); *Liquid Carbonic Co. v. Quick*, 25 A. B. R. 394, 182 Fed. 603 (C. C. A. Pa.); *Nat. Bank v. Carbon-dale, etc., Co.*, 27 A. B. R. 840, 195 Fed. 187 (C. C. A. Kan.); In *re Lutz*, 28 A. B. R. 649, 197 Fed. 492 (D. C. Ark.); In *re Appel Suit & Cloak Co.*, 28 A. B. R. 818, 198 Fed. 322 (D. C. Colo.); In *re Dancy, etc., Co.*, 28 A. B. R. 444, 198 Fed. 336 (D. C. Ala.).

31a. *Kenyon v. Mulert*, 26 A. B. R. 184, 184 Fed. 825 (C. C. A. Pa.).

on property fraudulently conveyed by a bankrupt.³² So as to deeds of trust;³³ likewise, as to the sufficiency of a transaction to effect an equitable assignment;³⁴ likewise, as to whether all creditors in bankruptcy may participate in the proceeds, upon recovery of fraudulently conveyed property, or only those existing at the time of the transfer.³⁵

Likewise as to exemptions;³⁶ and as to dower.³⁷

§ 1142. Detailed Discussion of Trustee's Title and Rights.—

In the preceding sections have been given a general discussion of the trustee's title and rights, from which has been derived the "Complete Statement" thereof with which the discussion opened. We now take up in detail these various rights of the trustee and discuss them in their order, bearing in mind not only that the subject is threefold, but also that there are subdivisions. Thus, we discuss the title and rights of the trustee, first, as successor to the bankrupt; second, as successor to creditors, finding this second class subdivided into three subclasses; and third, the peculiar rights conferred by the Bankruptcy Act itself, which we also find to be divided into three subclasses.

And, first, as to the title and rights of the trustee as successor to the bankrupt.

DIVISION 1.

TRUSTEE'S TITLE AND RIGHTS AS SUCCESSOR TO BANKRUPT'S TITLE AND RIGHTS.

§ 1143. First, Trustee's Title and Rights as Successor to Bankrupt's Title and Rights—Statement.—In accordance with the changes made by the Amendment of 1910, as previously noted in the discussion of §§ 1137 and 1139, the correct statement of the rights and title which the trustee takes as successor of the bankrupt's rights and title, now would be as follows:

The trustee succeeds to the bankrupt's title and stands in his shoes and has the bankrupt's rights and remedies, and also takes the property, in cases unaffected by any fraud of the bankrupt towards creditors, in the same plight and condition in which the bankrupt held it and subject to all equities and rights imposed upon it in the hands of the bankrupt, except where there has been some transfer or encumbrance of the property or seizure of it by legal process, void as against some creditor under State law to whose rights the trustee is subrogated, or void as against

32. In re Mullen, 4 A. B. R. 230, 101 Fed. 413 (D. C. Mass.).

33. Swager v. Smith, 27 A. B. R. 660, 194 Fed. 762 (C. C. A. W. Va.).

34. Goodwin v. Murchison Nat. Bank, 22 A. B. R. 703, 145 N. Car. 320.

35. See post, §§ 1225¾, 1738. In re Kohler, 20 A. B. R. 89, 159 Fed. 871 (C. C. A. Ohio), quoted at § 1225¾.

36. See ante, § 1041.

37. See post, §§ 1166, 1166½.

the trustee by some positive provision of the Bankruptcy Act, but as to the property in the custody or coming into the custody of the bankruptcy court, takes it in such plight and condition only to the extent that some creditor would have taken it had such creditor held a lien by legal or equitable proceedings thereon, and, as to property not in the custody of the bankruptcy court, held an unsatisfied execution.³⁸

The trustee, then, is bound by all the acts, contracts and conditions of

38. Bankr. Act, § 70 (a): "The trustee of the estate of a bankrupt, upon his appointment and qualification, and his successor or successors, if he shall have one or more, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of bankrupt, as of the date he was adjudged a bankrupt, except in so far as it is to property which is exempt, to all. * * *"

Bankr. Act, § 47 (a) (2), as amended in 1910: "And such trustees, as to all property in the custody or coming into the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies, and powers of a creditor holding a lien by legal or equitable proceedings thereon; and also, as to all property not in the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies, and powers of a judgment creditor holding an execution duly returned unsatisfied."

Also, §§ 67 (a) (b) (c) (d) (e) (f) and § 70 (e).

Before Amendment of 1910, However.—*Hewitt v. Berlin Machine Wks.*, 11 A. B. R. 709, 194 U. S. 296; *Humphrey v. Tatman*, 14 A. B. R. 75, 198 U. S. 91; (1867) *Donaldson v. Farwell*, 93 U. S. 631; (1867) *Casey v. Cavaroc*, 96 U. S. 467; obiter, *Linstroth Wagon Co. v. Ballew*, 18 A. B. R. 32, 149 Fed. 960 (C. C. A. Tex.); *Bank v. Rome Iron Co.*, 4 A. B. R. 448, 102 Fed. 755 (C. C. A. Ga.); (1867) *Hauselt v. Harrison*, 105 U. S. 401; *In re Cutting*, 16 A. B. R. 753, 145 Fed. 388 (D. C. N. Y.); instance, *Smith v. Mottley*, 17 A. B. R. 867 (C. C. A. Ohio); *In re Emslie*, 4 A. B. R. 128, 102 Fed. 291 (C. C. A. N. Y.); *In re Elmira Steel Co.*, 5 A. B. R. 487, 109 Fed. 456 (Special Master N. Y.); partially, *In re Kirby-Dennis Co.*, 2 A. B. R. 402, 95 Fed. 166 (C. C. A. Wis.); partially, *In re Standard Laundry Co.*, 8 A. B. R. 540, 116 Fed. 476 (C. C. A. Calif.). *In re Hurley*, 26 A. B. R. 434, 185 Fed. 851 (D. C. Mass.); *In*

re Lange Co., 20 A. B. R. 478, 159 Fed. 586 (D. C. Iowa); *Clay v. Waters*, 20 A. B. R. 560, 161 Fed. 815 (C. C. A. Mo.); *In re Grainer*, 20 A. B. R. 166, 160 Fed. 69 (C. C. A. Calif.); *Batchelder v. Wedge*, 19 A. B. R. 268, — Vt. —; (Security) *Warehousing Co. v. Hand*, 19 A. B. R. 291, 206 U. S. 415, quoted at § 1137; partially, *Richardson v. Shaw*, 19 A. B. R. 717, 209 U. S. 365; *Hurley v. Atchison R. Co.*, 22 A. B. R. 17, 213 U. S. 126, affirming 18 A. B. R. 396; impliedly, *In re Columbia Fireproof Door & Trim. Co.*, 21 A. B. R. 714 (D. C. N. Y.); partially, *In re Greek Mfg. Co.*, 21 A. B. R. 714, 164 Fed. 211 (D. C. Pa.); *Bryant v. Swafford Bros. Co.*, 22 A. B. R. 111, 214 U. S. 279, quoted at § 1140; *Corbitt Buggy Co. v. Ricand*, 22 A. B. R. 316, 169 Fed. 935 (C. C. A. N. C.); rule partly enunciated, *In re Proudfoot*, 23 A. B. R. 106, 173 Fed. 733 (D. C. W. Va.); *In re Meadows, Williams & Co.*, 23 A. B. R. 124, 173 Fed. 694 (D. C. N. Y.); *Godwin v. Murchison National Bank*, 22 A. B. R. 703, 145 N. Car. 320, 59 S. E. 154; *In re Clark Coal & Coke Co.*, 23 A. B. R. 273, 173 Fed. 658; 176 Fed. 955 (D. C. Pa.); *Crucible Steel Co. v. Hand*, 23 A. B. R. 302, 174 Fed. 127 (C. C. A. Ky.). Compare, *In re Fish Bros. Wagon Co.*, 21 A. B. R. 147, 164 Fed. 553 (C. C. A. Kans.). *In re MacDougall*, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.); *In re Automobile Livery Service Co.*, 23 A. B. R. 799, 176 Fed. 792 (D. C. Ala.); *In re Beihl*, 23 A. B. R. 905, 176 Fed. 583 (D. C. Pa.); *York Mfg. Co. v. Brewster*, 23 A. B. R. 474, 174 Fed. 566 (C. C. A. Tex.); *In re Bailey*, 23 A. B. R. 876, 176 Fed. 628, 176 Fed. 990 (D. C. S. Car.); *Mattley v. Wolfe*, 23 A. B. R. 673, 175 Fed. 619 (D. C. Neb. reversed in *Mattley v. Giesler*, 26 A. B. R. 116, 187 Fed. 970); *In re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.); *In re Walsh Bros.*, 28 A. B. R. 243, 195 Fed. 576 (D. C. Ia.); *Lovell v. Newman & Son*, 27 A. B. R. 746, 192 Fed. 753 (C. C. A. La.); *Gill, as Trustee v. Bell's Knitting Mills,*

the bankrupt's ownership (except such as would be invalid by State law as against some creditor or are void by the peculiar provisions of the Bankruptcy Act itself relative to preferential and fraudulent transfers and liens by legal proceedings within the four months) and the trustee has all the rights and is entitled to make all the defenses the bankrupt has. He "stands," under such circumstances, "in the shoes of the bankrupt."

Thus, if no circumstances exist that would have entitled a creditor, under the State law, to avoid the contract of the bankrupt or the lien upon his property, and if there was no preference nor lien obtained by legal proceedings within the four months preceding the bankruptcy and while the bankrupt was insolvent, then the trustee is bound and bound solely by the bankrupt's contracts and transfers, and this is so, no matter how onerous, how unprofitable, how improvident or unwise they may have been, being so bound to the same extent the bankrupt himself, or a general creditor of the bankrupt, would have been bound. His claims and interests in property are subject to all defenses, counterclaims, offsets, liens and rights that would have been available against the debtor had the debtor not been adjudged bankrupt.

Thompson v. Fairbanks, 13 A. B. R. 445, 196 U. S. 516 [decided before the Amendment of 1910]: "Under that law [of 1867] it was held that the assignee in bankruptcy stood in the shoes of the bankrupt, and that 'except where, within a prescribed period before the commencement of proceedings in bankruptcy, an attachment has been sued out against the property of the bankrupt, or where his disposition of his property was, under the statute, fraudulent and void, his assignees take his real and personal estate, subject to all equities, liens, and encumbrances thereon, whether created by act or by operation of law.' *Yeatman v. New Orleans Sav. Inst.*, 95 U. S. 674. See, also, *Stewart v. Platt*, 101 U. S. 731; *Hauselt v. Harrison*, 105 U. S. 401. Under the present Bankrupt Act, the trustee takes the property of the bankrupt, in cases unaffected by fraud, in the same plight and condition that the bankrupt himself held it, and subject to all the equities impressed upon it in the hands of the bankrupt, except in cases where there has been a conveyance or encumbrance of the property which is void as against the trustee by some positive provision of the Act."

York Mfg. Co. v. Cassell, 15 A. B. R. 637, 201 U. S. 344 [decided before the Amendment of 1910]: "Under the provisions of the Bankrupt Act the trustee in bankruptcy is vested with no better right or title to the bankrupt's property than belonged to the bankrupt at the time when the trustee's title accrued. At that time, the right, as between the bankrupt and the York Manufacturing Co., was in the latter company to take the machinery on account of default in the payment therefor. The trustee under such circumstances stands simply in the shoes of the bankrupt and as between them he has no greater right than the bankrupt."

24 A. B. R. 275, N. Y. App. Div., quoted at § 1728½; obiter, *In re Wade*, 26 A. B. R. 169, 185 Fed. 664 (D. C. Mo.).

Obiter, reaffirming rule but showing limitations, rule not applicable to

fraudulent transactions, though fraudulent merely "in law," *In re Standard Tel. & Elec. Co. (Knapp v. Milw. Tr. Co.)*, 24 A. B. R. 761, 216 U. S. 545. See §§ 1211, 1285.

In *re New York Economical Printing Co.*, 6 A. B. R. 615, 110 Fed. 514 (C. C. A. N. Y.) [decided before the Amendment of 1910]: "The Bankrupt Act does not vest the trustee with any better right or title to the bankrupt's property than belongs to the bankrupt or to his creditors at the time when the trustee's title accrues. The present Act like all preceding bankrupt acts, contemplates that a lien good at that time as against the debtor and as against all of his creditors shall remain undisturbed. If it is one which has been obtained in contravention of some provision of the Act, which is fraudulent as to creditors, or invalid as to creditors for want of record, it is invalid as to the trustee; and if it was one which was invalid as to some particular creditor, though valid as to other creditors, the trustee is in certain cases subrogated to the rights of that creditor."

In *re Blake*, 17 A. B. R. 669 (C. C. A. Mo.) [decided before the Amendment of 1910]: "A trustee in bankruptcy, in cases unaffected by fraud, and wherein no attachments nor executions have been levied upon the property of the bankrupt stands in the shoes of the latter and has no higher nor better rights."

In *re Garcewich*, 8 A. B. R. 152, 115 Fed. 87 (C. C. A. N. Y.) [Before Amendment of 1910]: "Under the present Bankrupt Act, as under previous bankrupt acts, the trustee takes the property of the bankrupt, in cases unaffected by fraud, in the same plight and condition that the bankrupt himself held it, and subject to all the equities impressed upon it in the hands of the bankrupt, except in cases where there has been a conveyance or incumbrance of the property which is void as against the trustee by some positive provision of the act."

Compare [1841] *Winsor v. McClellan*, 2 Story 492, Fed. Cas. 17,887 (C. C. Mass.): "Now the principle has been long established that the assignee in bankruptcy does not stand in the position of a purchaser, nor even in so favorable a position as an individual creditor may stand. 2 Story, Eq. Jur., §§ 1228, 1229, 1411; *Langton v. Horton*, 1 Hare 549, 563; *Muir v. Schenck*, 3 Hill, 228; *Murray v. Lylburn*, 2 Johns. Ch. 441, 443; *Deac. Bankr.* (Ed. 1827) pp. 320, 321, ch. 10, § 3. The assignee in bankruptcy takes the property of the bankrupt, in cases unaffected by fraud, in the same plight and condition that the bankrupt himself held it, and subject to all the equities which exists against the same in the hands of the bankrupt. This was clearly laid down by Lord Hardwicke in *Brown v. Heathcote*, 1 Atk. 160, 162, and has ever since been adhered to, not only in courts of equity, but also, as the case of *Leslie v. Guthrie*, 1 Bing. N. C. 697, abundantly shown, at law. But I need not dwell upon this point, as it comes very fully under consideration in the case of *Rand v. Winslow* (not reported), at the last October term of the Circuit Court in Maine."

[1841] *Mitchell v. Winslow*, 2 Story 630, Fed. Cases No. 9,673: "The present is a question between the assignee of a bankrupt, acting for the benefit of all the creditors, and the mortgagee, claiming title under his mortgage. * * * Now, it is most material to bear in mind under this aspect of the case, that it is a well-established doctrine that (except in cases of fraud), assignees in bankruptcy take only such rights and interests as the bankrupt himself had and could himself claim and assert, at the time of his bankruptcy, and consequently they are affected with all the equities which would affect the bankrupt himself if he were asserting those rights and interests. This was expressly laid down by Lord Hardwicke in *Brown v. Heathcote*, 1 Atk. 160, 162, where he said: 'The ground that the court go upon is this: that assignees of bankrupts, though they are trustees for the creditors, yet stand in the place of the bankrupt, and they can take in no better manner than he could.'"

[1867] *Yeatman v. Institution*, 95 U. S. 764: "The established rule is that, except in cases of attachment against the property of the bankrupt within a prescribed time preceding the commencement of proceedings in bankruptcy, and except in

cases where the disposition of property by the bankrupt is declared by law to be fraudulent and void, the assignee takes the title, subject to all equities, liens or encumbrances whether created by operation of law or by act of the bankrupt which existed against the property in the hands of the bankrupt."

[1867] *Stewart v. Platt*, 101 U. S. 731: "He takes the property in the same 'plight and condition' that the bankrupt held it. *Winsor v. McClellan*, 2 Story 492. The assignee can assert, in behalf of the general creditors, no claim to the proceeds of the sale of that property which the bankrupts themselves could not have asserted in a contest exclusively between them and their mortgagee."

In *re Great Western Mfg. Co.*, 18 A. B. R. 259, 152 Fed. 123 (C. C. A. Neb.) [Before Amendment of 1910]: "A trustee in bankruptcy stands in the shoes of the bankrupt, and has no better title than he, in the absence of fraud, or of attaching or judgment creditors at the time of the filing of the petition."

Crosby v. Miller, 16 A. B. R. 814 (Ct. Appl. D. C.) [Before Amendment of 1910]: "The assignee under the last Bankruptcy Act, and the trustee under the present bankruptcy law takes only such title as the bankrupt had subject to all equities. * * * There is no doubt that the trustee under the present law takes the title subject to all equities, liens or encumbrances, whether created by operation of law or by the bankrupt which existed against the property in the hands of the bankrupt."

Zartman, Trustee, v. Nat. Bank, 216 U. S. 134, 23 A. B. R. 635 (affirming 139 N. Y. 133) [Before Amendment of 1910]: "The trustee claims that he takes the same kind of title as a bona fide purchaser for value; but the rule applicable to this and all similar cases is that the trustee takes the property of the bankrupt, not as an innocent purchaser, but as the debtor had it at the time of the petition, subject to all valid claims, liens, and equities. *Tompson v. Fairbanks*, 196 U. S. 516, 13 Am. B. R. 437, * * * and cases cited. And this is so well settled that our jurisdiction of the writ of errors is exceedingly doubtful."

Davis v. Crompton, 20 A. B. R. 53, 158 Fed. 735 (C. C. A. Pa.) [Before Amendment of 1910]: "It has been often declared by the Supreme Court of the United States, that under the present Bankrupt Act, the trustee takes the property of the bankrupt in cases unaffected by fraud, in the same plight and condition that the bankrupt himself held it, and subject to all the equities impressed upon it in the hands of the bankrupt. It would seem that no other interpretation of § 70 of the act * * * consistent with the rights and vested interests of third parties, could be maintained. The trustee in a certain sense is the bankrupt. The bankrupt's title is his title, whether it be to things in possession or to choses in action. His title cannot rise higher than that of the bankrupt, so as to impinge upon or destroy the interest in or title to property, good as against the bankrupt himself. It is true, that, by the language of § 70, the trustee of the estate of the bankrupt is 'vested, by operation of law, with the title of the bankrupt, as of the date he was adjudged a bankrupt, * * * to all * * * (5) property which, prior to the filing of the petition, he could, by any means, have transferred, or which might have been levied upon and sold under judicial process against him.' But, taking the title of the bankrupt as it existed in him at the time of the adjudication, the trustee takes it subject to the superior title of the vendor. Otherwise, the title of the trustee would be superior to the title held by the bankrupt, and therefore not the title of the bankrupt to the property described in clause 5 of § 70, but one entirely different therefrom. It is this precise title, and no other, which is vested by operation of law, in the trustee."

Canning Machinery Co. v. Fuller, 20 A. B. R. 157, 158 Fed. 588 (C. C. A. Ala.) [Before Amendment of 1910]: "In considering these propositions, we have to

bear in mind that the respondent has no other title than the title the bankrupt had."

Atchison, etc., Ry. Co. v. Hurley, 18 A. B. R. 396, 153 Fed. 503 (C. C. A. Kans. affirmed 22 A. B. R. 17, 213 U. S. 126) [Before Amendment of 1910]: "The trustee stands in the shoes of the bankrupt. Whatever rights a third party had against the property of a bankrupt before adjudication, that party, in the absence of fraud or fixed liens created by State statutes in favor of others, has against his estate in bankruptcy." Quoted further at § 932.

In *re Chantler Cloak & Suit Co.*, 18 A. B. R. 498, 151 Fed. 952 (D. C. R. I.) [Before Amendment of 1910]: "The trustee in bankruptcy takes the property subject to all the equities imposed upon it in the hands of the bankrupt which are not invalid as to creditors."

In *re Mertens*, 15 A. B. R. 369, 142 Fed. 445 (C. C. A. N. Y.) [Before Amendment of 1910]: "Now the trustee takes the property of the bankrupt in the condition in which he finds it at the date of the adjudication, unless it has been incumbered fraudulently or in contravention of some of the provisions of the act."

Wood Co. v. Eubanks, 22 A. B. R. 307, 169 Fed. 929 (C. C. A. N. C.) [Before Amendment of 1910]: "It is well settled that the trustee of a bankrupt stands in the shoes of the bankrupt and occupies the same relation to the creditors that the bankrupt sustained prior to the date on which he was adjudged bankrupt."

In *re Hunt*, 14 A. B. R. 423, 139 Fed. 286 (D. C. N. Y.) [Before Amendment of 1910]: "A trustee in bankruptcy is not a purchaser in good faith nor does he occupy the position of such a purchaser. He takes the property of the bankrupt in cases not affected by fraud in the same plight and condition the bankrupt held it as of the date of the adjudication and subject to all equities impressed on it in the hands of the bankrupt, except in cases where there has been some conveyance or encumbrance void as against the trustee, made so by some positive enactment of the Bankruptcy Law. * * * He takes the title the bankrupt then had, no more, no less. Section 70, subd. (a). He takes title to such property charged with all liens and equities valid against the bankrupt unless, as just stated, they are made void or voidable by some positive provision of the Act. But in some cases liens may be avoided by the trustee that could not have been avoided by the bankrupt if the bankruptcy proceedings had not intervened."

Obiter, Gove v. Morton Trust Co., 12 A. B. R. 300 (Sup. Ct. N. Y. App. Div.) [Before Amendment of 1910]: "We suppose it will not be disputed that the trustee in bankruptcy takes the property of the bankrupt, subject to all liens and charges against it which might be enforced except for the provisions of the Bankruptcy Law."

In *re Foundry & Machine Co.*, 17 A. B. R. 293, 147 Fed. 828 (D. C. Wis.) [Before Amendment of 1910]: "By this provision the trustee takes no better title than the bankrupt had. Liens which were at that time valid against the bankrupt remain undisturbed. * * * A trustee in bankruptcy is vested with no better right than the bankrupt. He does not take property sold to the bankrupt by conditional sale with a reservation of title in the vendor. The property is subject to all equities impressed upon it in the hands of the bankrupt. A ruling of the United States Circuit Court of Appeals that a seizure by the Bankruptcy Court operates as an attachment and an injunction for the benefit of all the persons having interests in the property was reversed in *York Mfg. Co. v. Cassell*, 201 U. S. 344, 353, 15 Am. B. R. 633."

Partially, In *re Kellogg*, 10 A. B. R. 10, 112 Fed. 52 (C. C. A. N. Y.) [Before Amendment of 1910]: "The plaintiff, as trustee, stands in the shoes of the bankrupt. * * * He is the legal representative of the bankrupt."

Partially, *In re MacDonald*, 14 A. B. R. 804, 138 Fed. 463 (D. C. Conn.) [Before Amendment of 1910]: "Upon adjudication, the trustee took title to all property which was then vested in the bankrupt, subject to all valid claims, liens and equities."

Partially, *Duplan Silk Co. v. Spencer*, 8 A. B. R. 375, 115 Fed. 689 (C. C. A. Penn.) [Before Amendment of 1910]: "The trustee in bankruptcy, seeking by proceeding at law to enforce the title of the bankrupt to personal property so situated will be subject to all legal and equitable claims of others which exist against the bankrupt not in fraud of the Bankrupt Law or the rights of general creditors."

Partially, *In re Nicholas*, 10 A. B. R. 296, 122 Fed. 299 (D. C. N. Y.) [Before Amendment of 1910]: "The trustee in bankruptcy, on his appointment, took title to all the property on hand, subject to any rights of the appellant; but he took that title charged with all the liens, incumbrances and obligations existing against it, as they would have existed had all the property remained in the hands of the bankrupt, and he took no other or greater interest in the property, and no other or greater rights under the contract, than the bankrupt himself had."

In re Torchia, 26 A. B. R. 188, 185 Fed. 576 (D. C. Pa.): "Under the Bankruptcy Act of 1898, § 70, the trustee is vested with the title of the bankrupt mortgagor by act of law and not by the act of the bankrupt. The mortgagee is no nearer to the possession of the mortgaged premises after the election of the trustee than he was before. He could not have higher rights against the trustee than he had against the bankrupt. * * * The trustee stands in the shoes of the bankrupt. He could contest the right to the attorney's commission had he been made a party to the proceedings in the court in which the judgments were entered. He raised the objection before the referee upon distribution at the first opportunity, and his objections should have been sustained." [This case arose after the bankruptcy Amendments of 1910.]

But the bankrupt's title which is taken is subject, however, always to the qualification "except in cases where there has been a conveyance or encumbrance of the property which is void as against the trustee by some positive provision of the act."

In re McDonald, 23 A. B. R. 51, 173 Fed. 99 (D. C. Mass.): "But all this is always subject to the qualification expressly stated in *Thompson v. Fairbanks*, 196 U. S. 526, 'except in cases where there has been a conveyance or encumbrance of the property which is void as against the trustee by some positive provision of the act.'"

Or where there has been fraud of the bankrupt towards his creditors; or where the conveyance would be affected differently as to a "creditor armed with process."

§ 1144. Intervention of Creditors' Rights Causing Modification of Rule That Bankrupt's Title Taken.—In applying the principle of the trustee's succession to the bankrupt's title, it must not be forgotten that in many instances where it is said the bankrupt's title is the title taken, the rules of evidence as to the sufficiency of a transaction to effect a change of title, etc., will be different where creditors' rights have intervened from what it would be were the bankrupt's rights alone involved. This is notably so where the sufficiency or insufficiency of facts to constitute a delivery passing title is involved: what would amount to a

sufficient delivery to pass title as against the bankrupt alone might be insufficient where creditors' rights have intervened.³⁹

Again, what would amount to sufficiently clear proof of a resulting trust in favor of a wife, may be different where the rights of creditors become involved, as, for instance, where the husband becomes bankrupt.⁴⁰

Amendment of 1910 Giving Trustee Rights of Levying Creditor.—The Amendment of 1910, to Bankr. Act, § 47 (a), giving the trustee the rights of a levying creditor as to property in the custody, or coming into the custody, of the bankruptcy court, enables the trustee to take advantage, as to such property, of local law giving different rights where levying creditors' rights intervene.

In *re Franklin Lumber Co.*, 26 A. B. R. 37, 187 Fed. 281 (D. C. Pa.): "It is to be noted that § 47 (a) (2) as amended by the Act of June 25, 1910, applies to the present dispute. Under that amendment, if property coming into custody of the court be claimed by another, the trustee is vested with all the rights, remedies, and powers of a creditor holding a lien by legal or equitable proceedings thereon. An agreement therefore which would previously have been valid between the parties—such, for example, as was considered in *Davis v. Crompton* (C. C. A., 3d Cir.), 20 Am. B. R. 53, 158 Fed. 735 (209 U. S. 548)—is no longer necessarily valid against the trustee. He is in the position of a creditor holding a legal or equitable lien, and the agreement is to be scrutinized from that point of view.

"Assuming that the bankrupt would be bound by the words of this agreement and could not deny it to be a lease, his trustee is not so bound and may contend that the contract is really one of conditional sale. In such contention he may offer any competent and relevant evidence, and it is obvious I think that the conduct of the parties may ordinarily throw much light on the true meaning of their agreement. If they treat it as a contract of sale, it makes no difference what name they have given it. A creditor may adopt his own construction, and they cannot successfully object. This is well settled in Pennsylvania and elsewhere." This case is further quoted at §§ 1141 and 1228.

Since the passage of the Amendment of 1910, to the Bankruptcy Act, § 47 (a) (2), discussed heretofore in §§ 1137, 1139 and hereafter in § 1207, et seq., it is necessary to add the qualification, always, that the trustee, as thus bound by the bankrupt's sales, contracts, etc., is only bound thereby to the same extent that an existing creditor would be bound thereby under State law or a creditor whether actually existing or not, would be bound thereby had the latter levied legal or equitable process at the time the custody of the bankruptcy court arose over the property involved or had had an execution returned unsatisfied. So that, in considering all of the following paragraphs under this division and the cases cited thereunder, such qualification must always be borne in mind. Thus, in a State where a creditor of the bankrupt, had he been a levying creditor

39. *Alleman v. Hollander*, 11 A. B. R. 753, 128 Fed. 159 (D. C. Mass.); In *re Car & Locomotive W'ks*, 14 A. B. R. 331, 134 Fed. 919 (D. C. Ills.).

40. Compare, apparent instance, *Teter v. Viquesney*, trustee, 24 A. B. R. 242, 179 Fed. 655 (C. C. A. W. Va.).

(as to property in the custody of the bankruptcy court) or a creditor holding an execution returned unsatisfied (as to property not in its custody), would have better rights than the bankrupt himself possessed, then, in that State, the trustee would also possess such creditor's rights rather than be limited to those merely of the bankrupt.⁴¹

But the Amendment is not retroactive.⁴²

§ 1144¹. But Trustee May Abandon Burdensome Property or Unprofitable Contracts.—While it is true that the trustee is bound in his rights to property by the bankrupt's acts and contracts, he is not bound to accept burdensome property nor unprofitable contracts that would entail his performance of duties that would be burdensome to the estate; but he may refuse to accept or assume the same, leaving the other party to his remedy for the breach.⁴³

Atchison, etc., Ry. Co. v. Hurley, 18 A. B. R. 396, 153 Fed. 503 (C. C. A. Kans., affirmed in 213 U. S. 126, 22 A. B. R. 17): "It is well settled that trustees in bankruptcy are not bound to accept property or take over contracts which are onerous and unprofitable, and which would burden, rather than benefit, the estate. In the execution of their trust they are confronted at the outset with the duty of electing whether to assume an existing executory contract, continue its performance, and ultimately dispose of it for the benefit of the estate or to renounce it and leave the injured party to such legal remedies for the breach, as the case affords." Quoted further at §§ 1145, 1150½.

SUBDIVISION "A."

PROPERTY SUBJECT TO BANKRUPT'S SALES, MORTGAGES, CONVEYANCES,
DELIVERIES, BAILMENTS, CONTRACTS AND EQUITABLE LIENS.

§ 1145. Bound by Bankrupt's Sales, Mortgages, Deliveries, Bailments, Contracts and Equitable Liens.—Thus, the trustee in laying claim to property is bound by the terms of the bankrupt's sales or conveyances of it and of his covenants, contracts and acts in relation thereto as construed by state law, no matter how onerous, unprofitable or unwise they may be—save and except, always, as the same may be in fraud of creditors' rights or void as to creditors or be in contravention of statute.⁴⁴

41. Intervention of Creditor's Rights Causing Modification, etc.—Compare *In re Franklin Lumber Co.*, 26 A. B. R. 37, 187 Fed. 281 (D. C. Pa.), quoted at §§ 1141, 1228; *In re Waite-Robbins Motor Co.*, 27 A. B. R. 541, 192 Fed. 47 (D. C. Mass.).

42. *Arctic Ice Mach. Co. v. Armstrong Trust Co.*, 27 A. B. R. 562, 192 Fed. 114 (C. C. A. Pa.).

43. See ante, § 932; post, § 1150½. Also, see *Watson v. Merrill*, 14 A. B. R. 454, 136 Fed. 359 (C. C. A. Kans.), quoted at § 982; impliedly, *Kenyon v.*

Mulert, 26 A. B. R. 184, 184 Fed. 825 (C. C. A. Pa.).

44. *In re Marx Tailoring Co.*, 28 A. B. R. 147, 196 Fed. 243 (D. C. Ala.); *Sexton v. Kessler, etc., Co.*, 28 A. B. R. 85, 228 U. S. 634 (set out at § 1146); *In re Interstate Pav. Co.*, 28 A. B. R. 573, 197 Fed. 371 (D. C. N. Y.); *Ward v. First Nat. Bank*, 29 A. B. R. 312, 202 Fed. 609 (C. C. A. Ohio); *Rode & Horn v. Phipps*, 27 A. B. R. 827, 195 Fed. 414 (C. C. A. Tenn.); *Pyle v. Texas, etc., Co.*, 27 A. B. R. 225, 192 Fed. 725 (D. C. La.); *Lovell v. New-*

Atchison, etc., Ry. Co. v. Hurley, 18 A. B. R. 396, 153 Fed. 503 (C. C. A. Kans. affirmed in 213 U. S. 126, 22 A. B. R. 17): "Another and conclusive answer to the trustees' contention in this case is found in their conduct on assuming the duties of their trust. They found an assignable executory contract in force between the bankrupt and the railway company—one that might be advantageous or disadvantageous to the estate. It was evidenced by writing, but the parties had changed its mode of performance as already pointed out, so that as between them it consisted of the original instrument and the agreed modification. It is well settled that trustees in bankruptcy are not bound to accept property or take over contracts which are onerous and unprofitable, and which would burden, rather than benefit, the estate. In the execution of their trust they are confronted at the outset with the duty of electing whether to assume an existing executory contract, continue its performance, and ultimately dispose of it for the benefit of the estate or to renounce it and leave the injured party to such legal remedies for the breach, as the case affords. *American File Co. v. Garrett*, 110 U. S. 288, 295, * * * *Sparhawk v. Yerkes*, 142 U. S. 1, 13, * * * *Sessions v. Romadka*, 145 U. S. 29, * * * *Dushane v. Beall*, 161 U. S. 515, * * * *Watson v. Merrill*, 14 Am. B. R. 453, 136 Fed. 359, 363; *In re Chambers, Calder & Co.* (D. C.), 6 Am. B. R. 709, 98 Fed. 865; *Mercantile Trust Co. v. Farmers' Loan & Trust Co.*, 26 C. C. A. 383, 81 Fed. 254; *Central Trust Co. v. Continental Trust Co.*, 30 C. C. A. 235, 86 Fed. 517. If they elect to assume such a contract, they are required to take it cum onere, as the bankrupt enjoyed it, subject to all its provisions and conditions, 'in the same plight and condition that the bankrupt held it.'"

§ 1146. Thus, as to **Setting Apart or Delivery Sufficient to Pass Title to Goods Sold, Pledged or in Process of Manufacture, and "Warehousing."**—Thus, the trustee is bound by the sufficiency or insufficiency under State law of a setting apart or delivery by the bankrupt,⁴⁵ or of other acts, to pass title to goods pledged.⁴⁶

In *re Francis J. Bird*, 25 A. B. R. 24, 180 Fed. 229 (D. C. Minn.): "The important thing is, not that the property be in the possession of the creditor, but that it be out of the possession of the debtor."

man & Son, 26 A. B. R. 660, 188 Fed. 534 (C. C. La.); instance, *In re L. M. Alleman Hardware Co.*, 25 A. B. R. 331, 181 Fed. 810 (C. C. A. Pa.), reversing 22 A. B. R. 871; instance, *Mutual Life Insurance Co. v. Smith*, 25 A. B. R. 768, 184 Fed. 1 (C. C. A. Mass.); See post, §§ 1509, 1228; compare, § 1229.

Acts of Parties as Evidence of Meaning of Contracts.—The acts of parties in interest when they anticipate no trouble, are among the best criteria for interpreting the contracts they make. In *re Kessler & Co.*, 21 A. B. R. 583, 165 Fed. 508 (D. C. N. Y.).

Also when they have made a written contract in anticipation of trouble arising with creditors. In *re Hartman*, 26 A. B. R. 76, 185 Fed. 196 (D. C. N. Y.).

^{45.} In *re Kingston Realty Co.*, 19 A. B. R. 703, 157 Fed. 303 (D. C. N. Y.); delivery of key to mortgagee suf-

ficient though mortgagor also retaining another key, In *re Cole*, 22 A. B. R. 611, 171 Fed. 297 (D. C. R. I.).

Real Estate Deed to Wife but Kept in Husband's Custody Not in Effect Till Recorded.—Instance, *Prescott v. Galluccio*, 21 A. B. R. 229, 164 Fed. 618 (D. C. N. Y.).

Real Estate Deed Delivery Not to Take Effect Until Filed for Record.—An apparent delivery may be shown not to be the final delivery contemplated by the parties. *Ragan v. Donovan*, 26 A. B. R. 311, 189 Fed. 138 (D. C. Ohio).

^{46.} **Guarantee Title & Trust Co. v. First Nat. Bank**, 26 A. B. R. 85, 185 Fed. 373 (C. C. A. Pa.), wherein an assignment of an account "and the goods covered by or described therein" was held insufficient delivery to constitute a pledge under Pennsylvania law.

Instance, In *re Arkansas Fabric Mfg. Co.*, 18 A. B. R. 467, 151 Fed. 914 (D. C. Pa.); instance not sufficient to con-

Or to goods sold or manufactured.⁴⁷

Manufacturing Co. v. Lumber Co., 23 A. B. R. 595, 175 Fed. 335 (C. C. A. Mich.): "First, that the contract was for the sale of 'all of our cut 1907 of hemlock lumber at Ely, Mich.,' at the prices mentioned. Second, it was a sale upon credit of 60 days, with a discount of 2 per cent for cash, with privilege of vendor to require an advance of \$8,000, which was in fact made. Third, the lumber as cut was piled separate from other kinds and each length and width separate, as per the contract. * * * The construction of the contract and the determination of the matter of when title passed were questions of general law. And so was the question as to whether the parties had changed the contract, so as to pass the title at the yard, without delivery on the cars or preliminary inspection or measurement. The contract made no provision in respect to inspection to determine grade, nor as to measurement. If the parties elected to deliver without inspection or measurement, the title would pass if so accepted. The one essential thing was that the hemlock lumber then cut and piled should be then and there appropriated to this contract. In the absence of conditions to the contrary, the title would pass upon such appropriation subject to grading and measurement later as a preliminary to settlement of the price according to the written agreement."

stitute pledge of corporate stock, *French v. White*, 18 A. B. R. 905, 78 Vt. 89; instance, lack of original authority to execute, but corporation estopped from repudiation by retention of benefits, *In re Automobile Livery Service Co.*, 23 A. B. R. 799, 176 Fed. 792 (D. C. Ala.); instance not sufficient to constitute a second pledge by the pledgor of goods already pledged and in warehouse, *In re Roberts*, 21 A. B. R. 573, 166 Fed. 96 (C. C. A. Ills.); instance, pledge of whiskey in bonded warehouse, *Pattison v. Dale*, 27 A. B. R. 807, 196 Fed. 5 (C. C. A. Ohio).

Instance, pledging of life insurance policies, *Jones v. Coates*, 28 A. B. R. 249, 196 Fed. 860 (C. C. A. Mo.), decided under the law of Kansas.

47. *Guarantee Title & Trust Co. v. First Nat. Bank*, 26 A. B. R. 85, 185 Fed. 373 (C. C. A. Pa.); instance, sale of lumber, right of mortgagees, *Rode & Horn v. Phipps*, 27 A. B. R. 827, 195 Fed. 414 (C. C. A. Tenn.); instance, delivery of cotton to common carrier passes title, notwithstanding forgery, etc., of bill of lading, *Lovell v. Newman & Son*, 27 A. B. R. 746, 192 Fed. 753 (C. C. A. La.); instance, bailment under conditional sale not absolute sale, *Liquid Carbonic Co. v. Quick*, 25 A. B. R. 394, 182 Fed. 603 (C. C. A. Pa.).

Instance, tagging and setting apart of carriages at one end of wagon shop: *Allen v. Hollander*, 11 A. B. R. 755, 128 Fed. 159 (D. C. Mass.).

Instance, setting apart of locomotives sold but in process of repair: *In re Car & Locomotive Wks.*, 14 A. B. R. 331, 134 Fed. 919 (D. C. Ills.).

Instance, setting apart of lumber left on premises, under contract of sale of season's output: *Stelling v. G. W. Jones Lumber Co.*, 8 A. B. R. 521, 116 Fed. 261 (C. C. A. Wis.); instance, ties piled on railroad right of way and marked by agent, title passed, *McDonald v. Clearwater Ry. Co.*, 21 A. B. R. 182, 164 Fed. 1007 (U. S. C. C. Idaho).

Instance, motor truck, paid for in full by purchaser who received bill of sale, but actual delivery to be made when directions given, directions not being given until after bankruptcy, truck meanwhile retaining name of bankrupt painted on it, held title did not pass, *In re Waite-Robbins Motor Co.*, 27 A. B. R. 541, 192 Fed. 47 (D. C. Mass.).

Instance, setting apart of goods with statement that same sold, receipt being given: *In re Sherman Mfg. Co.*, 15 A. B. R. 740 (Ref. Mass.).

Instance, goods in process of manufacture: *In re MacDonald*, 14 A. B. R. 797, 138 Fed. 463 (D. C. Conn.).

Instance, sale for cash, delivery by mistake without payment: *Southern Pine Co. v. Savannah Trust Co.*, 15 A. B. R. 618, 141 Fed. 802 (C. C. A. Ga.).

Instance, where machinery was sold for cash and delivered to buyer on its promise to send a check forthwith, which it fails to do and thereafter the seller's agent accepts negotiable vouchers, secured by bonds, in payment and the buyer executes a lease—all the parties all the time acting in accordance with the idea that the title still remained in the seller—the title will be held still to be in the seller, *Canning Machinery*

Likewise, as to the sufficiency of facts to constitute "warehousing."⁴⁸ Where a part of the bankrupt's premises is used as a storage warehouse, under the name of an independent warehouse corporation, and warehouse receipts are issued on the bankrupt's goods therein, such facts have been held to convey a good title to the pledgee, no fraud being shown.⁴⁹ Also the delivery of a distilling company's own bonded warehouse receipt has been held to be sufficient delivery to consummate a pledge of whiskey, even though the warehouse were on the pledgor's own premises, by reason of the stringent regulations of the government.⁵⁰ But where there has been no actual change of possession, but a mere pretended change, the pledge will not be upheld.⁵¹

(*Security Warehousing Co. v. Hand*, 19 A. B. R. 291, 206 U. S. 415 (affirming S. C., 16 A. B. R. 49, 143 Fed. 42, C. C. A. Wis.): "The findings show that the receipts of the warehousing company were not entitled to the status of negotiable instruments, the transfer of which operates as a delivery of the property mentioned in them. Upon that question the case is sufficiently stated in the opinion of the court below, wherein it was said that the 'receipts themselves would put the holders on notice of the facts.' If the receipts were not negotiable instruments, it is contended that the transactions showed a valid pledge of the property to some of the appellants, and hence they are entitled to its possession until they are paid the debts due them from the bankrupt. Whether there was a sufficient change of possession of the thing pledged to render the same valid under the law of Wisconsin, we think was correctly answered in the negative by the courts below. *Geilfuss v. Corrigan*, 95 Wis. 651, 665, 669, 37 L. R. A. 166, 60 Am. St. Rep. 143, 70 N. W. 306. The general law of pledge requires possession, and it cannot exist without it. *Casey v. Cavaroc*, 96 U. S. 467 * * *. There was scarcely a semblance of an attempt at such change of possession from the hands of the knitting company to the hands of the warehousing company. Actual possession of the property in question was exercised by and existed with the knitting company substantially the same after the issuing of the receipts as before. It is a trifling with words to call the various transactions between the knitting company and the warehousing company a transfer of possession from the former to the latter. There was really no delivery, and no change of possession, continuous or otherwise. The alleged change was a mere pretense, a sham."

Fourth St. Nat. Bank v. Millbourne Mills Co., 22 A. B. R. 442, 172 Fed. 177 (C. C. A. Pa., affirming *In re Millbourne Mills Co.*, 20 A. B. R. 746, 162 Fed. 988, quoted at § 964): "The present case rises out of an attempt, by the bankrupt

Co. v. Fuller, 20 A. B. R. 157, 158 Fed. 588 (C. C. A. Ala.).

Instance, construed as trust agreement and not mortgage or conditional sale requiring record, *Wood Co. v. Eubanks*, 22 A. B. R. 307, 169 Fed. 929 (C. C. A. N. C.).

48. Compare as to construction of contract of "warehousing," *In re Nelson*, 27 A. B. R. 272, 191 Fed. 233 (D. C. S. Dak.), quoted at end of § 1146.

49. *Trust Co. & Warehouse Co. v. Wilson*, 14 A. B. R. 109, 198 U. S. 530; *Bush v. Export Storage Co.*, 14 A. B.

R. 138 (U. S. C. C. Tenn.); *Ward v. First Nat. Bank*, 29 A. B. R. 312, 202 Fed. 609 (C. C. A. Ohio); *Love v. Export Storage Co.*, 16 A. B. R. 171 (C. C. A. Tenn.).

50. *In re Miller Pure Rye Distilling Co.*, 23 A. B. R. 890, 176 Fed. 606 (D. C. Pa.).

51. *In re Rodgers*, 11 A. B. R. 79, 125 Fed. 691 (C. C. A. Ills., reversed for lack of summary jurisdiction sub nom. *Bk. v. Title & Tr. Co.*, 14 A. B. R. 102, 198 U. S. 280).

milling company, to pledge its property for money advanced, while still retaining possession and dominion over it. The form adopted was the issuing of so-called certificates, for so much grain or flour, in store at the mills, these certificates being issued to different parties, as collateral to loans, somewhat like ordinary warehouse receipts. The grain in question was contained in tanks, adjoining the mills, from which it was run to the mills, to be made into flour, by means of a conveyor, by simply unlocking a slide. It was drawn upon freely, in this way, no definite quantity being kept on hand, and there being no special arrangement with the holders of certificates, with regard to it, except that it was not to be reduced beyond the amount called for thereby. The fact is, that it was a shifting quantity, sometimes running far below this, although sometimes possibly above it. there being certificates outstanding at the time of bankruptcy for a hundred and thirty-eight thousand bushels, while there were but eighty-three thousand bushels on hand. The difference is ascribed to the depredation of insects, by which the grain became heated and lost weight, but it is difficult to see how fifty-five thousand bushels could have disappeared in that way. Nor is it material, the fact being, from whatever cause, that it was not there. The arrangement with regard to the flour was somewhat similar. It was stored in barrels in the basement of the company's warehouse under the charge of the superintendent, in three sections, two of two hundred barrels each, and one of eight hundred barrels, divided off from each other, by upright posts, and all bearing a certain common brand. There was also a sign that it was not to be touched by an employee; but aside from what this might vaguely imply, there was nothing to indicate that there was any control or ownership over it other than that of the bankrupt company in whose possession it was. Differing from the grain, there was no change in the quantity of the flour from the start; and certificates for the whole twelve hundred barrels were issued to the one bank. It is clear upon this showing, that the certificate holders have no case. The certificates, admittedly, cannot be sustained as warehouse receipts, however they may bear that form. A man cannot make a warehouse of himself as to his own goods. *Bank v. Jagode*, 186 Pa. 556; *Security Warehousing Co. v. Hand*, 206 U. S. 415, 19 Am. B. R. 291. Neither, there having been no delivery of the property, was there a valid pledge. The lien of a pledge, undoubtedly is preserved in bankruptcy. *Hiscock v. Varick Bank*, 206 U. S. 28, 18 Am. B. R. 1. But to have this so, the essentials of a pledge must appear, to which possession is indispensable, there being no lien as there is no pledge, without it."

Similarly, a bona fide sale of personal property by a debtor to another and a contemporaneous lease back at a rental to the seller, who, all the time, retained possession of the chattels, was held not to have passed title to the intended purchaser, for lack of delivery.

In *re Beihl*, 23 A. B. R. 905, 176 Fed. 583 (D. C. Pa.): "I see no difference in principle between this case and *Re Millbourne Mills Co.* (C. C. A., 3d Circuit), 20 Am. B. R. 746, 172 Fed. 177. There the milling company was the absolute owner of grain and flour in its own possession, and undertook to pledge it by issuing warehouse receipts, but without delivering the property itself. The attempted pledge was held to be invalid and of course therefore the absolute title had passed to the trustee. This is precisely what happened here. The bankrupt had an absolute title to the horses and wagons in his own possession, and undertook to pledge them by a somewhat round-about method, but without delivering the property. The bill of sale and the so-called lease and the parol contract concerning the payment of the past due claim for coal—taken together, as they

should be taken—clearly amount to a pledge or mortgage of the property. The bill of sale is equivalent to the deed, and the lease and parol agreement constitute the defeasance.”

Thus, a verbal assignment of book accounts where there was no manual delivery of any kind has been sustained in bankruptcy.⁵²

So, where the bankrupt set aside certain securities for the protection of a creditor prior to the four months period and during solvency entered the transaction on his books, and notified the creditor thereof, it was held that the delivery over to the creditor of such securities within the four months period was valid and binding on the trustee, notwithstanding that the securities were changed from time to time, and that the bankrupt was insolvent at the time of delivery.

Sexton v. Kessler & Co., 28 A. B. R. 85, 228 U. S. 634 (affirming S. C., 21 A. B. R. 807, 172 Fed. 535, C. C. A. N. Y., quoted post, § 1370): “It may be assumed that the arrangement between the parties was made in good faith and intended and believed to be valid, and, on the other hand, that at the time of the change of custody on October 23 within four months of the petition, the New York firm was insolvent and that the English Company had reasonable cause to believe that a preference was intended if its rights began only on that date.

“So far as the interpretation of the transaction is concerned, it seems to us that there is only one fair way to deal with it. The parties were business men acting without lawyers and in good faith attempting to create a present security out of specified bonds and stocks. Their conduct should be construed as adopting whatever method consistent with the facts and with the rights reserved is most fitted to accomplish the result. If an express declaration of an equitable lien, or again a statement that the New York firm constituted itself the servant of the English company to maintain possession for the latter, or that it held upon certain trusts, or that a mortgage was intended, or any other form of words would affect what the parties meant, we may assume that it was within the import of what was done, written or said. So that question is whether anything in the situation of fact or the rights reserved prevents the intended creation of a right in rem, or at least one that is to be preferred to the claim of the trustee.

“The Bankruptcy Law itself does not avoid the transaction (*Thompson v. Fairbanks*, 196 U. S. 516, 13 Am. B. R. 437; *Humphrey v. Tatman*, 198 U. S. 91, 95, 14 Am. B. R. 74). A trustee in bankruptcy does not stand like an attaching creditor; he gets no lien by the mere fact of his appointment (*York Mfg. Co. v. Cassell*, 201 U. S. 344, 15 Am. B. R. 633; *Zartman v. First National Bank of Waterloo*, 216 U. S. 134, 138, 23 Am. B. R. 635).” [This case arose before the Amendment of 1910 to § 47 (a) giving him the rights of a levying creditor.]

“The most obvious objection is that the continued physical power of the New York firm over the securities and its rights to withdraw and substitute admittedly reserved are inconsistent with a title or lien of the English house in any form. But the decisions of this court and of New York agree that there may be title in a stronger case than this. When a broker agrees to carry stock for a customer he may buy stocks to fill several orders in a lump; he may increase his single purchase by stock of the same kind that he wants for himself; he may pledge the whole block thus purchased for what sum he likes, or deliver it all in satisfaction

⁵². In re Macauley, 18 A. B. R. 459, 158 Fed. 322 (D. C. Mich.). Compare post, § 1147³⁴.

of later orders, and he may satisfy the earlier customer with any stock that he has on hand or that he buys when the time for delivery comes. Yet, as he is bound to keep stock enough to satisfy his contract, as the New York firm in this case was bound to substitute other security, if it withdrew any, the customer is held to have such an interest that a delivery to him by an insolvent broker is not a preference. *Richardson v. Shaw*, 209 U. S. 365, 19 A. B. R. 717; *Markham v. Joudon*, 41 N. Y. 235. So a depositor in a grain elevator may have a property in grain in a certain elevator, although the keeper is at liberty to mix his own or other grain with the deposit and empty and refill the receptacle twenty times before making good his receipt to the depositor concerned."

The preceding propositions must, of course, be taken with the qualification necessitated by the Amendment of 1910, that the trustee is bound by the bankrupt's title to be sure but, if the property be in the custody of the bankruptcy court, then he is bound only to the extent a creditor would have been bound had he levied legal process thereon, and if it be not in the custody of the court then only to the extent a creditor would have been bound thereby had he held an execution returned unsatisfied. Thus, as to attempted warehousings.

In re *Nelson*, 27 A. B. R. 272, 191 Fed. 233 (D. C. S. Dak.): "Applying its plain interpretation to this section and amendment, it follows that an agreement which would have been binding upon and could have been enforced between the parties hereto prior to the Amendment of 1910 no longer necessarily binds the trustee. His position is no longer the same as that of the bankrupt, but he is now in the position of a creditor holding a legal or equitable lien, and in this case the conditional sale of this property and the writing above set forth, termed a 'warehouse receipt,' are to be interpreted exactly as if the trustee were a creditor holding such lien."

§ 1147. Bankrupt's Contracts of Purchase or Sale, and His Mortgages.—Likewise, the trustee is bound by the terms of the bankrupt's purchases, sales⁵³ and mortgages.⁵⁴ Thus, as to "sale and return,"

⁵³. See cases cited in preceding section, § 1146; also see *In re Snelling*, 29 A. B. R. 818, 202 Fed. 259 (D. C. Mass.), wherein the court held that the rights of a third party occupying real estate under an oral contract of purchase were not affected by the Amendment of 1910, to Bankruptcy Act, § 47a(2).

Instance, corporation selling its stock for a patent right, the trustee cannot enforce any "unpaid stock subscription," for there is none unpaid, *Sternbergh v. (Duryea) Power Co.*, 20 A. B. R. 625, 161 Fed. 540 (C. C. A. Pa.); instance, contract of sale of season's output, *Mills v. Virginia-Carolina Lumber Co.*, 20 A. B. R. 750, 164 Fed. 168 (C. C. A. N. Car.).

Instance, *In re Millbourne Mills Co.*, 21 A. B. R. 363, 162 Fed. 988 (D. C.

Pa., affirmed sub nom. *Fourth St. Nat. Bk. v. Millbourne Mills Co.*, 22 A. B. R. 442, 172 Fed. 177 (C. C. A., quoted ante, at § 1146).

⁵⁴. See post, § 1229, et seq. Also, see instances, § 1146 note; also instance, conditional sale of newspaper press, and subsequent liens thereon, and as to whether by annexation other parts came under a chattel mortgage, *In re Atlanta Pub. Co.*, 20 A. B. R. 193, 160 Fed. 519 (D. C. Ga.); and also *In re Clark Coal & Coke Co.*, 23 A. B. R. 273, 173 Fed. 658, 176 Fed. 955 (D. C. Pa.).

Instance, mortgage given to indemnify surety company on bond given by bankrupt as depositor of school fund. *In re Silver*, 31 A. B. R. 106, 208 Fed. 797 (D. C. Ohio).

that is to say, a contract of sale with right to return;⁵⁵ likewise, as to purchases on approval;⁵⁶ likewise as to C. O. D. sales;^{56a} likewise, as to sales on payment;⁵⁷ likewise, where the bankrupt had refused to accept goods, though receiving them on the premises, claiming they did not comply with the contract of purchase;⁵⁸ likewise, as to sales where bill of lading is accompanied with draft.⁵⁹

Similarly, the trustee is bound by the bankrupt's acts where the lessee of a steam shovel continued to pay rent after the end of the year within which an option to purchase was to be exercised.⁶⁰ Likewise, as to "leases" of personal property, where not in fraud of creditors' rights.⁶¹ Similarly, where a draft and its accompanying bill of lading have fallen into different hands.⁶² Likewise, as to the relation between an "agent" and a manufacturer, etc.⁶³ Thus, where delivery on a cash sale was made without insistence on the cash, though ten days later an invoice retaining title in the vendor was sent, the court held a waiver had been made.⁶⁴ Thus, as to chattel mortgages and other securities to cover a floating balance of indebtedness;⁶⁵ and, as to the validity of chattel mortgages,⁶⁶ and, as to after-acquired property coming under a mortgage.⁶⁷ Also, as to mortgages on real estate to cover future advances, and as to what advances are covered thereby;⁶⁸ and similarly, as to goods on consignment⁶⁹ and as to

55. Instances, *In re Miller & Brown*, 14 A. B. R. 439, 135 Fed. 868 (D. C. Pa.); *In re Nicholas*, 10 A. B. R. 291, 122 Fed. 299 (D. C. N. Y.); *In re Schindler*, 19 A. B. R. 800, 158 Fed. 458 (D. C. N. Y.); *In re Landis*, 18 A. B. R. 483, 151 Fed. 896 (D. C. Pa.).

56. *Pridmore v. Puffer Mfg. Co.*, 20 A. B. R. 851, 163 Fed. 496 (C. C. A. S. Car.). Instance, *In re Paper Co.*, 17 A. B. R. 121, 147 Fed. 858 (D. C. Pa.), wherein held that after delay of year too late to deny title in bankrupt; instance, *In re Kingston Realty Co.*, 19 A. B. R. 703, 157 Fed. 303 (D. C. N. Y.); *In re Landis*, 18 A. B. R. 483, 151 Fed. 896 (D. C. Pa.).

56a. Instance, *Guarantee Title & Trust Co. v. First Nat. Bank*, 26 A. B. R. 85, 185 Fed. 373 (C. C. A. Pa.).

57. *In re Kingston Realty Co.*, 19 A. B. R. 703, 157 Fed. 303 (D. C. N. Y.); *Pridmore v. Puffer Mfg. Co.*, 20 A. B. R. 851, 163 Fed. 496 (C. C. A. S. C.).

58. *In re Planett Mfg. Co. (Schultz v. Scott)*, 19 A. B. R. 729, 157 Fed. 916 (C. C. A. Ind.).

59. *In re Reboulin Fils*, 21 A. B. R. 296, 165 Fed. 245 (D. C. N. Y.).

60. *McEwen v. Totten*, 21 A. B. R. 336, 164 Fed. 837 (C. C. A. Ga.).

61. *Nyles v. Am. Trust & Sav. Bank*, 21 A. B. R. 535, 166 Fed. 276 (C. C.

A. Ills.). Also, compare post, § 1228, et seq.

62. *In re Kessler & Co.*, 21 A. B. R. 583, 165 Fed. 508 (D. C. N. Y.).

63. *In re Sassman*, 21 A. B. R. 893, 167 Fed. 419 (D. C. Pa.); instance, *Parlett v. Blake*, 26 A. B. R. 25, 188 Fed. 200 (C. C. A. Mo.).

64. Instance, *Guarantee Title & Trust Co. v. First Nat. Bank*, 26 A. B. R. 85, 185 Fed. 373 (C. C. A. Mo.).

65. Instance, *In re Williams*, 9 A. B. R. 731, 120 Fed. 38 (D. C. Ga.); *Rode & Horn v. Phipps*, 27 A. B. R. 827, 195 Fed. 414 (C. C. A. Tenn.).

66. Instance, *In re Foundry & Machine Co.*, 17 A. B. R. 291, 147 Fed. 828 (D. C. Wis.); instance, *In re Grain-ger*, 20 A. B. R. 166, 160 Fed. 69 (C. C. A. Calif.).

67. Instances, *In re Sentenne & Green Co.*, 9 A. B. R. 648, 120 Fed. 436 (D. C. N. Y.); *In re Adamant Plaster Co.*, 14 A. B. R. 815, 137 Fed. 251 (D. C. N. Y.); *In re Dry Dock Co.*, 16 A. B. R. 325 (C. C. A. N. Y.); *National Bank v. Carbondale, etc., Co.*, 27 A. B. R. 840, 195 Fed. 180 (C. C. A. Kan.).

68. *Hendricks v. Webster*, 20 A. B. R. 112, 159 Fed. 927 (C. C. A. N. Y.).

69. *In re Bailey*, 23 A. B. R. 876, 176 Fed. 628, 176 Fed. 990 (D. C. S. Car.); *York Mfg. Co. v. Brewster*, 23 A. B. R. 474, 174 Fed. 566 (C. C. A. Tex.). Also, see post, § 1228.

the bankrupt's pledges.⁷⁰

Again, in accordance with this rule the vendee's equitable interest in land for the purchase price already paid, will be protected where the seller's bankruptcy prevents the seller from completing the contract.⁷¹ And the validity and effect of a deed of trust securing an annuity to a wife, where a decree for alimony was subsequently changed to such arrangement by agreement, although the parties subsequently remarried, was decided in accordance with the bankrupt's rights under State law; and accumulated interest thereon was held not allowable.⁷² The question as to whether a certain transaction amounted to a "novation" or a mere substitution, where the purchaser of a plant took up an old mortgage and gave a new one covering more property, was decided in accordance with the bankrupt's rights under State law.⁷³

Thus, also, as to whether chattel mortgages are void for indefiniteness has been decided in accordance with the State law.⁷⁴

And the bankrupt estate has been held bound by the bankrupt's husband's signing of the bankrupt's name to a conditional sale contract, although the seller supposed himself to be dealing with the husband and that the signature was the husband's own signature.⁷⁵

And the assumption by the executive officers of a bankrupt corporation, of the functions of a board of directors with the acquiescence of the stockholders, has been held to bind the corporation and hence to bind the trustee.⁷⁶

The interest on mortgages is also included within the protection of the law; for the trustee takes title to mortgaged property subject to the mortgage debt including interest, the bankruptcy adjudication not operating to cut off the interest.⁷⁷

Coder v. Arts, 18 A. B. R. 513, 152 Fed. 943 (C. C. A. Iowa, affirmed in 22 A. B. R. 1, 213 U. S. 223): "By the terms of the note and mortgage the mortgagor agreed to pay interest on his debt until it was paid * * *. The covenant for the sale and the application of the proceeds of these lands to the payment of the debt and interest was valid and binding, and it ran with the land, so that when the latter came into the hands of the trustee it was mortgaged for the payment of the interest as much as for the payment of the principal. * * * Another rule might prevail if the proceeds of the mortgaged property were insufficient to pay the mortgaged debt and its interest in full and the mortgagee was seeking to collect an unpaid balance by sharing with

70. Instance, *Guarantee Title & Trust Co. v. First Nat. Bank*, 26 A. B. R. 85, 185 Fed. 373 (C. C. A. Mo.); *In re Automobile Livery Service Co.*, 23 A. B. R. 799, 176 Fed. 792 (D. C. Ala.); *In re Miller Pure Rye Distilling Co.*, 23 A. B. R. 890, 176 Fed. 606 (D. C. Pa.). See also, ante, § 1146.

71. Instance, *In re Peasley*, 14 A. B. R. 496, 137 Fed. 190 (D. C. N. H.).

72. *Savage v. Savage*, 15 A. B. R. 599, 114 Fed. 346 (C. C. A. Va.).

73. See ante, § 1206¼. Instance,

Long v. Gump, 16 A. B. R. 501 (C. C. A. Ohio).

74. Instances, *In re Beede*, 11 A. B. R. 387, 120 Fed. 853 (D. C. N. Y.); *Davis v. Turner*, 9 A. B. R. 704, 120 Fed. 605 (C. C. A. N. Y.).

75. Instance, *In re Burkle*, 8 A. B. R. 542, 116 Fed. 766 (D. C. Conn.).

76. Instance, *Cunningham v. Germ. Ins. Bk.*, 4 A. B. R. 367, 101 Fed. 977 (C. C. A. Ky.).

77. See also, §§ 598, 758½, 1997½.

other creditors in the distribution of the common property. He might not be entitled then to recover from the proceeds of the common property interest upon his debt to any later date than the unsecured creditors would recover interest upon their claims."

So as to property held by the bankrupt and another person as tenants in common.⁷⁸ So as to building and loan association mortgages.⁷⁹

Certificates of stock bought and paid for by a customer belong to the customer and the trustee must surrender them.⁸⁰

The trustee is also bound by federal statutes where they would be applicable had no bankruptcy intervened; and so an assignment of a valid claim against the United States Government has been held absolutely void, under U. S. Rev. Stat., § 3477, for lack of formal acknowledgment, witnesses, etc.⁸¹

§ 1147¹/₂. Conditional Sales.—Likewise, the trustee is bound by the bankrupt's contracts of conditional sale.⁸²

§ 1147³/₄. Assignment of Book Accounts and Notice to Debtors.—Successive assignments of book accounts by the bankrupt from time to time, under an arrangement whereby the assignee advances money up to a certain percent of their face value, the bankrupt continuing to collect the accounts in his own name, though as agent of the assignee and accounting to him therefor, are effective to transfer the title to the accounts even though no notice is given to the debtors; nor is the arrangement itself fraudulent in law, where it is not actually fraudulent and where neither party knows of the bankrupt's insolvency.

Greedy v. Dockendorff, 231 U. S. 513, 31 A. B. R. 407 (affirming 103 Fed. 475): "The case was referred to a special master, who found that it did not appear that either the petitioner or the bankrupt knew that the latter was insolvent at the time of the supposed preference, or that there were any transfers with intent to defraud creditors, and found for the petitioner. His finding of facts and conclusions were concurred in by the District Court and Circuit Court of Appeals (203 Fed. Rep. 475, 121 C. C. A. 597). But no sufficient reason is shown for departing from our ordinary rules, where the master, the court of first instance, and the Circuit Court of Appeals have agreed, and in the course of the hearing this was admitted. * * *

"The trustee relies upon the general application of the lien under the agreement as constituting a fraud in law. Whatever effect it might have as evidence must be laid on one side in view of the findings below. The question here is

78. *In re McConnell*, 28 A. B. R. 659, 197 Fed. 438 (D. C. N. Y.).

79. *In re Davis*, 25 A. B. R. 1, 180 Fed. 148 (D. C. N. Y.).

80. *In re Meadows, Williams & Co.*, 24 A. B. R. 251, 177 Fed. 1004 (C. C. A. N. Y., affirming 23 A. B. R. 124, 173 Fed. 694).

81. *Guarantee Title & Trust Co. v. First Nat. Bank*, 26 A. B. R. 85, 185 Fed. 373 (C. C. A. Mo.).

82. *National Bank v. Williams*, 20

A. B. R. 79, 159 Fed. 615 (C. C. A. Tex.); instance, *In re Max Cohen*, 20 A. B. R. 796, 163 Fed. 444 (D. C. N. Y.); *Pridmore v. Puffer Mfg. Co.*, 20 A. B. R. 851, 163 Fed. 496 (C. C. A. S. C.; *Crucible Steel Co. v. Holt*, 23 A. B. R. 302, 174 Fed. 127 (C. C. A. Ky.). Instance, *In re Grainger*, 20 A. B. R. 166, 160 Fed. 69 (C. C. A. Calif.), though here the court's order of payment of remaining price held unauthorized. Also, see post, §§ 1228, 1241, 1242, 1244, 1263, 1878.

whether successive assignments of accounts by way of security, in pursuance of a contract under which advances were made to enable the assignor to get the goods on the faith of the undertaking that the accounts should be assigned, were bad because the contract embraced all accounts, although neither party contemplated any fraud. The rule of the English statutes as to reputed ownership may extend to debts growing due to the bankrupt in the course of his business, but we have no such statute. The advances were the means by which the bankrupt got the ownership of the goods. The contract of itself would operate as a conveyance as soon as the rights to which it applied were acquired. *Field v. New York*, 6 N. Y. 179. We do not see why in the interval between the acquisition of the goods and the specific assignment of accounts the right of general creditors without lien should intervene to defeat a security given in good faith when, but for the promise of it, the property never would have come into the bankrupt's hands. There may have been a moment when the goods could have been attached, or when, if insolvency had been made known, as in *National City Bank v. Hotchkiss* (U. S. Sup. Ct.), 31 Am. B. R. 291, it would have been too late to make the promised lien good. But in this case the lien was acquired before any knowledge of insolvency and before any attachment intervened. See *Jaquith v. Alden*, 189 U. S. 78, 9 Am. B. R. 773; *Coder v. Arts*, 213 U. S. 223, 22 Am. B. R. 1; *Van Iderstine v. Nat. Discount Co.*, 227 U. S. 575, 583, 29 Am. B. R. 478. It is objected that this lien was secret. But notice to the debtors was not necessary to the validity of the assignment as against creditors (*Williams v. Ingersoll*, 89 N. Y. 508, 522), and merely keeping silence to the latter, whether known or unknown, created no estoppel. *Wiser v. Lawler*, 189 U. S. 260, 270; *Ackerman v. True*, 175 N. Y. 353, 363. There was no active concealment and no attempt to mislead any one interested to know the truth.

"We content ourselves with this very general answer to an argument that dealt with many details that we have not mentioned, because those details were material only to a reconsideration of the findings of fact. Probably a hope of securing such a reconsideration was one of the inducements towards bringing the case here."

The Supreme Court of the United States in the case of *Greey v. Dockendorff* above quoted indicates strongly, however, that such an arrangement might well be found to be fraudulent in fact, though not fraudulent as matter of law; and it cannot be doubted that, if the arrangement for the advance is made on the express understanding that it shall be kept secret and that notice shall not be given to the debtors who owe the accounts, it is such activity as would warrant a conclusion of actual fraud.

The English doctrine of "Reputed Ownership" makes the failure to give notice to the debtors, where accounts receivable are assigned by way of security, equivalent to a failure to deliver tangible chattels to a pledgee or mortgagee thereof, whose rights as against levying creditors, as well as against bona fide purchasers or encumbrancers would be forfeited unless the instrument of transfer were recorded, where possession is not actually changed and the former owner is left the ostensible owner. But such is not the rule in the United States, where the recording acts, relative to transfers of personal property, have been held not to apply to choses in action but only to tangible property.

A verbal assignment of book accounts where there is no manual delivery

of any kind, has been sustained in bankruptcy.^{82a} In accordance with the rule, notice to debtors whose debts on book accounts have been assigned by the bankrupt as collateral security has been held not essential to the validity of the assignment.^{82b}

On the other hand, it has been held that the assignment of a debt requires for its validity as to third parties notice to the debtor, but not acceptance by him.^{82c}

A verbal assignment by way of mortgage or pledge of book accounts to be after acquired, as security for present endorsement by relatives has been upheld in accordance with the rights of the parties under state law.^{82d}

But, at any rate, mere notices at the bottom of invoices authorizing remittances to be made to third parties have been held not to be assignments of accounts to such parties.^{82e}

§ 1148. Bankrupt's Assumption of Mortgage or Other Obligation.—The trustee is bound by the bankrupt's assumption of mortgages,⁸³ or other obligations.⁸⁴

§ 1149. Estoppels against Bankrupt, Good against Trustee.—Estoppels good against the bankrupt and not invalid against levying creditors had there been no bankruptcy, are good against the trustee.⁸⁵

^{82a}. In re Macauley, 18 A. B. R. 459, 158 Fed. 322 (D. C. Mich.).

^{82b}. Young v. Upson, 8 A. B. R. 377, 115 Fed. 192 (D. C. N. Y.).

^{82c}. In re Wilson, 23 A. B. R. 814 (D. C. Hawaii).

^{82d}. Instance, Union Trust Co. v. Bulkeley, 18 A. B. R. 35, 150 Fed. 510 (C. C. A. Mich.).

^{82e}. Ryttenberg v. Schaefer, 11 A. B. R. 653, 131 Fed. 313 (D. C. N. Y.).

⁸³. Instance, chattel mortgage assumed by bankrupt, trustee may not question validity; In re Standard Laundry Co., 8 A. B. R. 538, 116 Fed. 476 (C. C. A. Calif., affirming 7 A. B. R. 254); instance, In re Beaver Knitting Mills, 18 A. B. R. 528, 154 Fed. 320 (C. C. A. N. Y.); In re Fire Proof Door & Trim Co., 21 A. B. R. 714, 168 Fed. 159 (D. C. N. Y.).

⁸⁴. Instance, held no assumption, In re Baumblatt, 18 A. B. R. 496, 153 Fed. 485 (D. C. Pa.).

⁸⁵. In re Naylor Mfg. Co., 14 A. B. R. 284, 135 Fed. 206 (D. C. Pa.). Instance, estoppel to deny authority of president to bind bankrupt corporation by lease of machinery purchased by his authority, Canning Machinery Co. v. Fuller, 20 A. B. R. 157, 158 Fed. 588 (C. C. A. Ala.). Vendee of cash register under conditional sale selling to another, his levy is not effective to avoid contract afterwards. In re Greek Mfg.

Co., 21 A. B. R. 714, 164 Fed. 211 (D. C. Pa.); Pyle v. Texas, etc., Co., 27 A. B. R. 225, 192 Fed. 725 (D. C. La.); Aldine Trust Co. v. Smith, 25 A. B. R. 608, 182 Fed. 449 (C. C. A. Pa.).

Instance, In re Automobile Livery Service Co., 23 A. B. R. 899, 176 Fed. 792 (D. C. Ala.), wherein the court held that the trustee, succeeding to the bankrupt's title, was estopped from urging the original lack of authority on the part of the corporate officers to make the pledge, by retention of the consideration received therefrom.

But compare, apparently contra, In re Laundry Co., 23 A. B. R. 859, 176 Fed. 740 (D. C. N. Y.), wherein the court held that the renewal of a chattel mortgage given by a corporation for borrowed money, where the assent of two-thirds of the stockholders had not been obtained as required under the New York statute, was invalid as against the trustee, though the bankrupt itself would have been estopped.

Notes, Secured by Accounts, in Turn Transferred as Collateral by Holder, under Representation.—Instance, banking firm's trustee in bankruptcy estopped from claiming that proceeds of accounts pledged with it by a bankrupt merchant should be paid to the banking firm's trustee rather than to banks to which the banking firm had transferred the merchant's notes under

§ 1149½. **Right of Subrogation.**—The right of subrogation, in accordance with the ordinary rules of equity, is unimpaired.⁸⁶

Thus, the trustee takes the property subject to the right of subrogation of one paying off liens thereon, where such right of subrogation would have existed against the bankrupt.^{86a} Again, he takes it subject to the rights of the bankrupt's children, who had surrendered to their father life insurance policies for specific purposes, to subrogation to certain mortgages paid off through misuse of the policies.^{86b}

§ 1150. **Specific Contractual Rights and Equitable Liens.**—Specific contractual rights (where recording is not necessary) and equitable liens and assignments created by the bankrupt are binding on the trustee,⁸⁷ if binding on the bankrupt by State law and not void as in fraud of creditor's rights^{87a} nor in contravention of the Bankruptcy Act.^{87b}

Thus, where an owner had a right by specific contract to use material left on the premises by a building contractor, it was held that title to the material did not pass to the trustee.⁸⁸ Again, an equitable lien on property already pledged (or already subject to an equitable lien by contract) and in a third person's hands, was held valid without delivery to the equitable lienors, the trustee's rights being held to be those of the bankrupt under State law.⁸⁹

Again, where a contract to furnish certain articles provides that, until sold, or paid for in cash, they should remain the seller's property, and, when sold, all proceeds of the sale, including cash, notes, etc., should be kept separate as a trust fund and be turned over to the seller as collateral security, the seller's rights are unimpaired by the bankruptcy.⁹⁰

the representation that they were secured by the accounts. In re Milne, 26 A. B. R. 10, 185 Fed. 244 (C. C. A. N. Y.).

86. In re Bruce, 19 A. B. R. 770, 158 Fed. 123 (D. C. N. Y.); In re Automobile Livery Service Co., 23 A. B. R. 799, 176 Fed. 792 (D. C. Ala.); In re MacDougall, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.). Also, see post, § 2278, et seq.

86a. In re Automobile Livery Service Co., 23 A. B. R. 799, 176 Fed. 792 (D. C. Ala.).

86b. In re MacDougall, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.).

87. In re Forse, 25 A. B. R. 843, 182 Fed. 212 (D. C. N. Y.); In re De Long Fur Co., 26 A. B. R. 469, 188 Fed. 686 (D. C. Pa.); In re M. E. Dunn & Co., 28 A. B. R. 127, 193 Fed. 212 (D. C. Ark.); Sexton v. Kessler & Co., 28 A. B. R. 85, 228 U. S. 634 (set out at § 1146). Instance, no equitable lien proved: Ryttenberg v. Schefer, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.). But are void if in fraud of creditor's rights, see §§ 1209 et seq. es-

pecially § 1222½; In re Liberty Silk Co., 18 A. B. R. 582, 152 Fed. 844 (D. C. N. Y.). In re Bellevue Pipe & F'd'y Co., 22 A. B. R. 97, 16 Ohio Dec. 247 (Ref. Ohio).

Equitable Lien Defined.—See post, § 1878; also, see In re Max Goldman, 23 A. B. R. 497, 174 Fed. 579 (C. C. A. Ohio); In re Wilson, 23 A. B. R. 814 (D. C. Hawaii).

87a. Same subject discussed under "Trustee's Rights as Successor to Creditors," post, § 1222½, where fraud involved.

87b. Same subject discussed where fraud not necessarily involved but levying creditor exists, post, § 1253½.

88. Duplan Silk Co. v. Spencer, 8 A. B. R. 367, 115 Fed. 689 (C. C. A. Penn., reversing 7 A. B. R. 563).

89. McDonald v. Daskam, 8 A. B. R. 543, 116 Fed. 276 (C. C. A. Wis., affirming In re Veneer & Panel Co., 6 A. B. R. 275); Bank v. Rome Iron Co., 4 A. B. R. 441, 102 Fed. 755 (U. S. C. C.).

90. In re McGehee, 21 A. B. R. 656, 166 Fed. 928 (D. C. Ga.).

Likewise, as to equitable assignments of insurance policies: the trustee stands in the bankrupt's shoes. Thus, an agreement made at the time of commencing a line of credit, to procure and assign to the creditor policies of fire insurance covering the goods to be purchased therewith, operates as an equitable assignment and is valid in bankruptcy.⁹¹ Likewise, an oral agreement to insure for the benefit of a mortgagee will operate as an equitable lien upon the proceeds of a fire insurance policy taken out by the mortgagor in his own name;⁹² but not as an equitable lien upon the proceeds of a policy taken out by the grantee of the equity of redemption.⁹³

It has been held that an equitable assignment of a part of a fund will not operate as against a trustee or receiver in bankruptcy, unless the debtor or fundholder has notice of it.⁹⁴ And the validity of an assignment of future earned wages has been decided (at any rate as to wages earned before bankruptcy, where such assignment is not void as a preference) in accordance with general law.⁹⁵

Thus, equitable liens upon standing timber, created by verbal agreement before the four months period, have been held valid as against the trustee, the bankrupt's potential interest in the logs and timber being held sufficient.⁹⁶

Again, where a mining company was under contract to supply a railway company with coal, but became embarrassed, and the railway company thereupon advanced it money to meet its pay roll on the oral agreement that such money should be advance payment for the coal, an equitable pledge was thereby created of the unmined coal which the Supreme Court upheld in bankruptcy.

Hurley v. Atchison Ry. Co., 22 A. B. R. 17, 213 U. S. 126: "Equity looks at the substance, and not at the form. That the coal for which this money was advanced was not yet mined, but remained in the ground to be mined and delivered from day to day, as required, does not change the transaction into one of an ordinary independent loan on the credit of the coal company or upon express mortgage security. It implies a purpose that the coal, as mined, should be delivered, and is, from an equitable standpoint, to be considered as a pledge of the unmined coal to the extent of the advancement. The equitable rights of the parties were not changed by the commencement of bankruptcy proceedings. All obligations of a legal and equitable nature remained undisturbed thereby. If there had been no bankruptcy proceedings, the coal as mined was, according to the understanding of the parties, to be delivered as already paid for by the advancement."

So, also, the rights of the trustee, where a seller claims under contract

91. *Wilder v. Watts*, 15 A. B. R. 57, 138 Fed. 423 (D. C. S. C.); *In re Grandy & Son*, 17 A. B. R. 206 (D. C. S. C.); *McDonald v. Daskam*, 8 A. B. R. 543, 116 Fed. 276 (C. C. A. Wis.). Also, see post, §§ 1253, 1370.

92. *Hanson v. Blake & Co.*, 19 A. B. R. 325, 150 Fed. 342 (D. C. Me.).

93. *Hanson v. Blake & Co.*, 19 A. B. R. 325, 150 Fed. 342 (D. C. Me.). Also, see post, §§ 1253, 1370.

94. *In re The Leader*, 26 A. B. R. 668, 190 Fed. 624 (D. C. Ark.).

95. *Mallin v. Wenham*, 13 A. B. R. 210, 209 Ills. 252. Compare, *In re West*, 11 A. B. R. 782, 128 Fed. 205 (D. C. Oregon). See ante, § 451; post, § 2662.

96. *Mercantile & Stock Co. v. Gallo-way*, 19 A. B. R. 244, 156 Fed. 504 (D. C. Ore.).

a lien on timber not yet cut, have been decided in accordance with the rights of the bankrupt under State law.⁹⁷

And, similarly, where a bona fide contract of purchase of a lumber mill's entire output is in existence, on which moneys have been advanced to the seller, the delivery of lumber thereunder, though on the eve of the seller's bankruptcy, is valid.⁹⁸

Likewise, a contract providing that lumber as manufactured was to be "applied upon the contract," has been held to give rise to an equitable lien upon the lumber afterwards manufactured.⁹⁹

A bona fide pledgee of stock standing in the bankrupt's name, will be protected though the stock was originally subscribed for the bankrupt's father who afterwards died before completing payment, the bankrupt completing payment with his own funds and taking the stock in his own name, though executor of his father's estate.¹

Likewise, in accordance with the rule, a draft drawn by a landlord on his agent for future rents to be collected and discounted at bank, has been held to operate as an equitable assignment of the rents as they later accrued and to be good against the landlord's trustee in bankruptcy.²

Similarly, the trustee's right to the proceeds of the sale of the bankrupt's seat in a stock exchange is subject to the lien of creditor members, under the rules of the exchange.⁴

A building contract stipulating against liens and duly recorded has been held, in accordance with the state law, to bar liens in Pennsylvania.⁵ And, in accordance with general law, where an agreement for a contemporaneous mortgage has been disregarded and goods commingled, the seller has been held to have a lien on the entire mass for the purchase price.⁶

A six months' delay in carrying out an agreement, made contemporaneously with delivery, to give later a lease or conditional sales contract, has been held not to invalidate the lease or contract when executed.⁷ And the wife's right to the proceeds of corporate stock held as security, where by State law she is incapacitated to contract, has been decided in accordance with State law.⁸

Similarly, liens created by an agreement to secure "by the goods themselves" have been upheld.¹¹ And an equitable lien before four months has

97. Instance, *In re Muncie Pulp Co.*, 18 A. B. R. 60, 151 Fed. 732 (C. C. A. N. Y.).

98. *Mills v. Virginia & Carolina Lumber Co.*, 20 A. B. R. 750, 164 Fed. 168 (C. C. A. N. Car.).

99. *Gage Lumber Co. v. McEldowney*, 30 A. B. R. 251, 207 Fed. 255 (D. C. Ky.), quoted at § 1372.

1. *In re McCord*, 23 A. B. R. 164, 174 Fed. 820 (C. C. A. N. Y.).

2. *In re Oliver*, 12 A. B. R. 694 (D. C. Tex.).

4. *In re Gregory*, 23 A. B. R. 270, 174 Fed. 629 (C. C. A. N. Y.).

5. *Ludowici Tile Roofing Co. v. Penn. Inst.*, 8 A. B. R. 739 (D. C. Penn.).

6. *In re Hennis*, 17 A. B. R. 889 (Ref. N. Car.).

7. *In re Hutchins*, 24 A. B. R. 647, 179 Fed. 864 (D. C. N. Y.).

8. *Tucker v. Curtin*, 17 A. B. R. 354, 148 Fed. 929 (C. C. A. Mass.).

11. *In re Louis Levin*, 21 A. B. R. 665, 173 Fed. 119 (D. C. N. Y.); to same effect, *Wood Co. v. Eubanks*, 22 A. B. R. 307, 169 Fed. 929 (C. C. A. N. C.), wherein the court held that a provision in a contract, under which certain machinery and implements were sold

been held created, though delivery was not made until within four months.¹²

Where equitable assignments have been made by bankrupts of parts of funds due them as contractors from owners, the rights of the trustee have been decided in bankruptcy in accordance with the State law.¹³ But a mere promise by a government contractor, made before the four months period, to pay a subcontractor with the money expected from the government on an estimate, will not constitute an "equitable assignment" of the money.¹⁴ And in accordance with the main proposition, it has been held, that, where a bank has refused payment of the check of the bankrupt because of rumors of his failure, the holder has no right to the deposit but that the deposit should be ordered paid over to the trustee.¹⁵

But the reservation of secret charges or liens upon property are not to be upheld as "equitable liens" to which the property is to be considered subject in the hands of the trustee, where they amount to a fraud upon the law.¹⁷ And the essentials of an equitable lien must exist, else it will not be sustained as such;^{17a} thus, where a vendor's lien is claimed the essentials of such a lien must exist.^{17b}

An equitable assignment has been defined to be any writing or act which shows an intention to transfer the specific funds in the hands of another, the same being completed when notice is given to the fund holder.¹⁸

An equitable assignment of a bankrupt legatee's interest in his ancestor's estate, not yet actually paid over, is not created by the mere written agreement of a prior assignee thereof to pay to another creditor any surplus over and above his own debt and other prior liens and costs and expenses.

In *re Ballantine* [*Clase v. Worth*], 26 A. B. R. 275, 186 Fed. 91 (C. C. A. Pa.): "The case differs therefore from the cases to which we have been referred in which appropriations out of expectancies which have subsequently come into

to a bankrupt, that "all goods on hand, and the proceeds of all sales of goods received under this contract, whether such proceeds of sales consist of notes, cash or book accounts, the party of the second part agrees to hold as collateral security in trust and for the benefit of the party of the first part, until all obligations hereunder due party of the first part from the party of the second part are paid in cash," constituted a trust, valid as against the bankrupt's trustee, and was neither a mortgage nor a contract of conditional sale, and under the law of the State was not required to be registered.

12. *Godwin v. Murchison National Bank*, 22 A. B. R. 703, 145 N. Car. 320.

13. Building contract, *Ludowici Tile Roofing Co. v. Penn Inst.*, 8 A. B. R. 739 (D. C. Penn.); Building contract, *In re Hanna & Kirk*, 5 A. B. R. 127,

105 Fed. 587 (D. C. Penn.); Paving contract, *In re Cramond*, 17 A. B. R. 23 (D. C. N. Y.).

14. In *Smedley v. Cpeckman*, 19 A. B. R. 694, 157 Fed. 815 (C. C. A. Pa.).

15. In *re Grive*, 18 A. B. R. 202, 151 Fed. 711 (D. C. Conn.). However, compare, post, § 1681.

17. In *re Liberty Silk Co.*, 18 A. B. R. 582, 152 Fed. 844 (D. C. N. Y.), quoted at § 1222½.

17a. Compare post, §§ 1222½, 1253½; also see *Fourth St. Nat. Bk. v. Millbourne Mill Co.*, 22 A. B. R. 442, 172 Fed. 177 (C. C. A. Pa.); compare, *In re Southern Textile Co.*, 23 A. B. R. 170, 174 Fed. 523 (D. C. N. Y.).

17b. In *re Teter*, 23 A. B. R. 223, 173 Fed. 798 (D. C. W. Va.).

18. In *re Wilson*, 23 A. B. R. 814 (D. C. Hawaii).

existence have been upheld as equitable assignments. Here Ballantine had a vested life interest in the two estates over and above all that had been assigned by him to the finance company and others. He assigned no part of that remaining interest to the appellees. He simply authorized the finance company, if at any future time it should receive money on his account in excess of what he owed to it and certain other parties, to pay out of that excess the claims of appellees."

An assignment of a subcontract for furnishing and setting tile for buildings, as collateral security for borrowed money, has been held not to pass title to the tile itself, the wording of the contract being insufficient.²⁰

Similarly, patented articles left with the bankrupt to be sold under license—the trustee is bound by the terms of the license.²¹

That a wife's delivery of money to her husband is presumptively a gift has been decided in accordance with State law; likewise, whether sufficient proof exists to establish a resulting trust in favor of a wife in lands bought in her husband's name, has been decided in accordance with general rules of law.²⁴

So as to the assignment of contracts entered into with a municipality for paving.²⁵

In one case where notes had been given by a merchant from time to time to a banking firm for money which the banking firm used in paying the merchant's debts, taking the accounts of the merchant's customers as security and afterwards the banking firm in turn itself pledged the notes with a bank under the representation that they were secured by good accounts and merchandise, it was held, upon the ultimate bankruptcy of both the merchant and the banking firm, that the latter's trustee was not entitled to the proceeds of the merchant's account for the banking firm's own creditors, but at best merely to hold as a trustee in equity, for the benefit of the banks.²⁶

A bank's ownership will be protected where it accepts and pays drafts for the purchase price of goods imported and receives bills of lading which it then exchanges for trust receipts of the purchaser who agrees therein to hold the goods as security for the advances or to sell them and apply the proceeds on the bank's claim, the bank reserving the right at any time to cancel the trust and take possession of the goods.²⁷

In *re Cattus*, 26 A. B. R. 348, 183 Fed. 733 (C. C. A. N. Y.): "The course of dealing between the bank and the bankrupt is according to commercial usage of long standing, under which by a loan of credit a vast amount of business is rapidly and safely done. The particular steps of the method followed are not always the same, but the substantial feature which makes the banker the owner of the goods until the purchase price of them advanced by him is paid is always

20. In *re Wilson & Co.*, 23 A. B. R. 907, 176 Fed. 652 (D. C. Pa.).

21. In *re Spitzel & Co.*, 21 A. B. R. 729, 168 Fed. 156 (D. C. N. Y.).

24. *Teter v. Visquesney*, trustee, 24 A. B. R. 242, 179 Fed. 655 (C. C. A. W. Va., affirming In *re Teter*, 23 A. B. R.

223, 173 Fed. 798).

25. In *re Interstate Pay. Co.*, 28 A. B. R. 573, 197 Fed. 370 (D. C. N. Y.).

26. In *re Milne*, 26 A. B. R. 10, 185 Fed. 244 (C. C. A. N. Y.).

27. In *re Coe*, 26 A. B. R. 352, 183 Fed. 745 (C. C. A. N. Y.).

present. One common method, which seems to have been adopted in this case, is as follows: A merchant who wishes to import goods for which he has not funds to pay obtains credit from a bank to a fixed amount, against which he draws for the price of the goods to the order of the vendor or the vendor draws for the price to his own order. The draft with bill of lading indorsed in blank or to the order of the bank is forwarded by the vendor to the banker for acceptance. The banker accepts the draft payable in one, two, three, or four months, as the case may be, forwards the bill of lading indorsed in blank to his agent in New York, who delivers the same to the importer against a receipt called a trust receipt, whereby he agrees to sell the goods for account of the banker, to pay him the proceeds and so put him in funds to take up the acceptance at maturity. * * * The purpose of the parties, describe the trust receipt as you will, was to keep the title to the goods in the bankers until their acceptances for the price of the goods were paid. The courts, without always defining exactly what the relation between the parties is or always defining it in the same way, still are astute to protect the rights of the banker in such case. * * * It would be most inequitable that the bankrupt or his trustee should escape from the performance of this obligation for the benefit of any one except a bona fide purchaser for value or creditors protected by statute."

Thus, the trustee is bound by the bankrupt's previous transfer of all his property to another person to sell and apply upon the claims of all creditors except certain ones named;²⁸ that is to say, of course, unless such transfer be invalid for fraud or as being an assignment for the benefit of creditors within four months of the bankruptcy.

It has been held that a third party in possession of real estate under claim of equitable right thereto by virtue of an oral contract is not affected by the Amendment of 1910 to Bankruptcy Act, § 47 (a) (2).^{28a}

§ 1150½. Oral Modifications of Written Contracts Unknown to Trustee.—The trustee, in the absence of fraud, is bound by valid modifications of written contracts made by the bankrupt before adjudication, whether such modifications were known to the trustee or not.

Atchison, etc., Ry. Co. v. Hurley, 18 A. B. R. 396, 153 Fed. 503 (C. C. A. Kans., affirmed sub nom. *Hurley v. Atchison, etc., Ry. Co.*, 22 A. B. R. 17, 213 U. S. 126): "Any valid modifications of a written contract which may have been made by the bankrupt before adjudication, whether oral or in writing, and whether known or unknown to the trustees, are binding upon them if they elect to assume and perform the contract. They take it subject to all equities between the original parties. *Reeves v. Kimball*, supra; *Wood v. Donovan*, 132 Mass. 84; *Homer v. Shaw*, 177 Mass. 1, 58 N. E. 160; *Mangles v. Dixon*, 3 H. of L. Cas. 703. The duty rests upon the trustees to make inquiry and ascertain the true nature, character, and conditions of the contract before exercising their election. When the election is made to assume it where no fraud has been practiced upon them, they stand in exactly the same situation as the bankrupt himself stood prior to the adjudication. *Cases*, supra. After presumably making all the inquiries necessary to fully acquaint themselves as to the advisability

²⁸. *Gill v. Bell's Knitting Mills*, 21 A. B. R. 282, 128 N. Y. App. Div. 601, 24 A. B. R. 275 (N. Y. App. Div.), quoted at § 1728½.

^{28a}. *In re Snelling*, 29 A. B. R. 814, 202 Fed. 258 (D. C. Mass.).

of taking over the executory contract in question the trustees in this case determined to do so, assumed the contract and entered upon its execution. They mined coal, delivered it to the railway company, and, in the language of the trial court, 'performed fully all the terms of the contract as it was written,' but failed to conform to the condition created by the oral agreement to deliver coal to the railway company in payment of the advances made by it to keep the mine going." Quoted further ante, § 1145.

§ 1151. Forfeiture Clauses, Rent, etc.—The trustee is bound by all forfeiture clauses and rent covenants of the bankrupt. Thus, where forfeiture of a long term lease was declared before bankruptcy for failure to build as covenanted, the trustee is bound by the forfeiture and the bankruptcy court will enforce it.²⁹ But he may urge that forfeiture has been waived by the conduct of the parties.³⁰

§ 1152. Fixtures.—The trustee takes the property under the bankrupt's rights as to fixtures.

Thus, it has been held by the bankruptcy court, in accordance with local or general law, that a steam engine was not a fixture; yet, if so, that the vendor's lien thereon was entitled to priority and that the trustee had no right thereto until the balance of the purchase price was tendered by him;³¹ and the bankrupt vendee's right to remove alleged fixtures, where the contract preserves certain rights of removal, has been decided in accordance with local law;³² thus, if the fixtures are such that, under the local law, or the provisions of the lease, they belonged to the landlord, the tenant's trustee is not vested therewith;³³ and whether a lien on realty covers certain fixtures and is entitled to participate in the distribution of a fund derived from a sale thereof, will also be decided in accordance with the law of the State.³⁴

§ 1152½. After-Acquired Property.—The trustee stands in the bankrupt's shoes as to after-acquired property and as to the right to the increase of property, etc.

Mercantile & Stock Co. v. Galloway, 19 A. B. R. 244, 156 Fed. 504 (D. C. Ore.): "Another suggestion is that it was incompetent for the parties thus to impose a lien upon after-acquired property. It is sufficient answer to this that Buck had at least a potential interest in the logs and lumber, and it is believed that it was competent for him to affix the lien, looking first to the manufacture of such logs and lumber; the timber out of which the product was to be manufactured being his by indisputable purchase."

Except, always, of course where creditors under State law have greater rights, as to which see post, § 1207, et seq.

²⁹ *Lindeke v. Associates Realty Co.*, 17 A. B. R. 215 (C. C. A. Minn.).

³⁰ *In re Palatable Water Co.*, 18 A. B. R. 833, 154 Fed. 531 (D. C. Pa.); *Mound Mines Co. v. Hawthorne*, 23 A. B. R. 242, 173 Fed. 882 (C. C. A. Colo.).

³¹ *In re Smith*, 9 A. B. R. 590 (D. C. R. I.).

³² *Instance, In re Rodgers & Hite*, 16 A. B. R. 401 (D. C. Pa.). See ante, § 1000.

³³ *In re Bahl, etc., Co.*, 28 A. B. R. 139, 195 Fed. 986 (D. C. Pa.).

³⁴ *In re Beeg*, 25 A. B. R. 572, 184 Fed. 522 (D. C. Pa.).

§ 1153. Disregarding Note and Suing on Original Consideration.

—The trustee may disregard a note and sue upon the original consideration, under the same circumstances and subject to the same limitations as the bankrupt.³⁵

SUBDIVISION "B."

MECHANICS' AND SUBCONTRACTORS' LIENS, LANDLORDS' LIENS AND SIMILAR LIENS.

§ 1154. **Mechanics' and Subcontractors' Liens, Landlords' Liens, etc.**—Mechanics' and Materialmen's liens and kindred liens, properly evidenced by affidavit duly filed and recorded, where requisite, and valid under the State law as against the bankrupt, in general are valid against the trustee, and he takes the property subject to them.³⁶

§ 1155. **Mechanics' Liens, etc., Not Liens Obtained by Legal Proceedings nor Preferences.**—A mechanic's lien is not a lien obtained

35. Instance, *In re Jackson*, 2 A. B. R. 501, 94 Fed. 797 (D. C. Vt.).

36. *In re Beck Prov. Co.*, 2 N. B. N. & R. 532 (Ref. Ohio); *In re Emslie*, 2 N. B. N. & R. 922, 4 A. B. R. 126, 102 Fed. 291 (C. C. A. N. Y.), reversing 3 A. B. R. 282, 516; *Howard v. Cunliff*, 10 A. B. R. 71, 69 S. W. 737 (Mo. Ct. Appeals); *George Carrol & Bros. Co. v. Young*, 9 A. B. R. 645, 119 Fed. 576 (C. C. A. Penna.); *In re Kirby-Dennis Co.*, 2 A. B. R. 402, 95 Fed. 116 (C. C. A. Wis., affirming 2 A. B. R. 218, 94 Fed. 818); *In re Georgia Handle Co.*, 6 A. B. R. 472, 109 Fed. 632 (C. C. A. Ga.); *In re Grissler*, 13 A. B. R. 508, 136 Fed. 754 (C. C. A. N. Y.); *Mott v. Wissler Min. Co.*, 14 A. B. R. 321, 135 Fed. 697 (C. C. A. Va.); *In re Falls City Shirt Mfg. Co.*, 3 A. B. R. 437, 98 Fed. 592 (D. C. Ky.); *In re Franklin*, 18 A. B. R. 218, 226, 151 Fed. 642 (D. C. N. Car.); *Crane Co. v. Smythe*, 11 A. B. R. 747, 87 N. Y. Supp. 917; compare, *In re Huston*, 7 A. B. R. 95 (Ref. since District Judge N. Y.); *In re Hobbs & Co.*, 16 A. B. R. 544, 145 Fed. 211 (C. C. A. W. Va.); *obiter*, *Moore v. Green*, 16 A. B. R. 653, 145 Fed. 480 (C. C. A. W. Va.); *impliedly*, *In re Cramond*, 17 A. B. R. 22 (D. C. N. Y.); *impliedly*, *In re Lynn Camp Coal Co.*, 22 A. B. R. 60, 168 Fed. 998 (D. C. Ky.); *In re New England Breeders' Club*, 23 A. B. R. 689, 175 Fed. 501 (D. C. N. H.). See ante, § 1145.

Instance, *In re Gosch*, 9 A. B. R. 613, 126 Fed. 627 (D. C. Ga., reversed on other grounds, in 12 A. B. R. 149):

Sash and door factory not a "saw-mill" within Georgia lien law.

Instance, *Chauncey v. Dyke Bros.*, 9 A. B. R. 444, 119 Fed. 1 (C. C. A. Ark., affirming, with modifications, *In re Matthews*, 6 A. B. R. 96, 109 Fed. 603): Mechanics' liens in Arkansas having priority over prior mortgage unless prior mortgage given to raise money to make the improvements for which mechanics' liens arose.

Instance, *In re West Norfolk Lumber Co.*, 7 A. B. R. 648, 112 Fed. 759 (D. C. Va.): Mechanics' liens and liens for supplies under Virginia Supply Lien Act not liens upon proceeds of insurance policies, upon burning of buildings unless by express agreement.

Instance, *In re Oconee Mill Co.*, 6 A. B. R. 475, 109 Fed. 866 (C. C. A. Ga.): Special lien for furnishing machinery and repairs for mill, under Georgia law is entitled to preferential payment from proceeds of sale of the property, provided the claim of lien was duly recorded.

Instance, whether a turpentine still is "machinery" within Georgia Mechanics' Lien Law, *In re Anderson*, 21 A. B. R. 413 (Ref. Ga.).

Instance, mechanics' lien superior to corporate bond mortgage, *In re Park Coal & Coke Co.*, 23 A. B. R. 273, 173 Fed. 658, 176 Fed. 955 (D. C. Pa.).

Verbal Notice to Owner under Ohio Law.—Whether the notice to the owner of the filing of lien affidavit may be verbal, see *In re Boner*, 26 A. B. R. 321, 189 Fed. 92 (D. C. Ohio).

through legal proceedings.³⁷

Obiter, Henderson v. Mayer, 225 U. S. 631, 28 A. B. R. 387: "But the statute was not intended to lessen rights already existing, nor to defeat those inchoate liens given by statute, of which all creditors were bound to take notice and subject to which they are presumed to have contracted when they dealt with the insolvent. Liens in favor of laborers, mechanics and contractors are of this character; and although they may be perfected by record or foreclosure within four months of the bankruptcy, they are not created by judgments, nor are they treated as having been obtained through legal proceedings, even when it is necessary to enforce them by some form of legal proceedings. The statutes of the various states differ as to the time when such liens attach, and also as to the property they cover. * * * In some cases the lien dates from the commencement of the work or from the completion of the contract. In others, prior to the levy, they are referred to as being dormant or inchoate liens, or as 'a right to a lien.' In *re Bennett*, 18 A. B. R. 320, 153 Fed. 677; In *re Laird*, 6 A. B. R. 1, 109 Fed. 550. But the courts, dealing especially with bankruptcy matters, have almost uniformly held that these statutory preferences are not obtained through legal proceedings, and therefore, are not defeated by § 67 f, even where the registration, foreclosure, or levy, necessary to their completion or enforcement, was within four months of the filing of the petition in bankruptcy." Quoted further at § 1160.

Nor is it a lien given by way of preference to secure a pre-existing debt.³⁸ It comes under none of the heads of those liens or conveyances or transfers that are void as against the trustee in bankruptcy. Such a mechanic's lien, rather, comes under the exception of clause (d) of § 70, which provides that.

"Liens given or accepted in good faith and not in contemplation of or in fraud upon this act, and for a present consideration, which have been recorded

³⁷. See post, subject of "Nullification of Liens Obtained by Legal Proceedings," § 1437. See *Howard v. Cunliff*, 10 A. B. R. 71, 69 S. W. 737 (Mo. Ct. App.; In *re Beck Prov. Co.*, 2 N. B. N. & R. 532 (Ref. Ohio); In *re Emslie*, 4 A. B. R. 126, 102 Fed. 291 (C. C. A. N. Y., reversing on this point 3 A. B. R. 282 and 516); In *re Kirby-Dennis Co.*, 2 A. B. R. 402, 95 Fed. 116 (C. C. A. Wis., affirming 2 A. B. R. 218, 94 Fed. 818); *Mott v. Wissler Min. Co.*, 14 A. B. R. 321 (C. C. A. Va.); *obiter*, *Moore v. Green*, 16 A. B. R. 653 (C. C. A. W. Va.); In *re Cramond*, 17 A. B. R. 32 (D. C. N. Y.); *obiter*, In *re Robinson & Smith*, 18 A. B. R. 563, 154 Fed. 343 (C. C. A. Ills.); In *re New England Breeders' Club*, 23 A. B. R. 689, 175 Fed. 501 (D. C. N. H.).

Contra, In *re Monroe Lumber Co.*, 24 A. B. R. 371, 186 Fed. 252 (D. C. Miss.): "Where the laborers of a saw mill corporation which had been placed in the hands of receivers in the state court, with suspension of operations, instituted proceedings in such court to

establish a lien for their services upon all the property of the corporation, which proceedings were pending in said court at the time of the adjudication in bankruptcy of said corporation no lien had been so fixed as that the adjudication did not nullify." But this case is not well reasoned. The state statute referred to seems clearly to have provided for a definite lien as a substantive right, the legal proceedings not creating the lien but merely enforcing it. However, if the state courts have held that it was not a "lien" but a mere "priority," then the rules of § 2197, post, would probably apply. See post, §§ 1437, 1444, 1586, 2196, 2197 and 2198.

³⁸. In *re Emslie*, 4 A. B. R. 126, 102 Fed. 291 (C. C. A. N. Y., affirming on this point 3 A. B. R. 282, 516); In *re Beck Prov. Co.*, 2 N. B. N. & R. 532 (Ref. Ohio). To same general effect, In *re Lynn Camp Coal Co.*, 22 A. B. R. 60, 168 Fed. 998 (D. C. Ky.); In *re New England Breeders' Club*, 23 A. B. R. 689, 175 Fed. 501 (D. C. N. H.).

according to law if record thereof is necessary in order to impart notice, shall not be affected by this act."³⁹

This becomes plain when one comes to reflect upon the nature of a mechanic's lien. A mechanic's lien arises by operation of law and, according to the law of most, if not all, of the States, begins with the first stone laid, the first nail driven or the first load of material dumped on the premises. It grows as the edifice grows and expands with the development of the work. It is there in an inchoate form from the beginning. It is essentially and clearly a lien arising upon a presently passing consideration, and must be assumed to have been in the contemplation of the parties engaged in the work both as owners and contractors. Therefore, such a lien is one given and accepted upon a present consideration, and is within the meaning of clause (d) of § 70, and is not a preference nor a lien obtained by legal proceedings. Moreover, such a lien is good against creditors under the State law, so is not void for want of record. Even if the bankruptcy of the owner occurs before the lien affidavit is filed, the lien is not affected in most States so long as the affidavit is filed at some time within the statutory period for filing, although after the adjudication of bankruptcy; for the filing of the affidavit does not, in most States, create the lien—it simply prolongs it. It is merely the statutory notice of the lien that must be given some time within the prescribed period after the completion of the work in order to continue the notice after the newness of the work itself has worn off and ceased to be a reminder of the rights of those who have done the work.⁴⁰

Obiter, *Moore v. Green*, 16 A. B. R. 653, 145 Fed. 211 (C. C. A. W. Va.): "The lien here claimed is analogous to that of mechanics, materialmen, sub-contractors, etc., which class of liens have been respected and enforced under the present Bankruptcy Act. They are given a lien by statute, but to be effective the same must be preserved and secured within a prescribed period by filing such claims, duly perfected, etc., for recordation in the designated court of the State. Being thus entitled to this inchoate lien, taking the steps to secure the benefit thereof within four months of bankruptcy has in every instance, so far as we are advised, been held not to be the taking of legal proceedings in contravention of the Act, but merely doing the necessary thing—taking the essential step—to secure the existing right under the statute. In this class of claims, by reason of the work done or supplies furnished under the agreement between the parties, the statute declares that there shall exist for the amount due a lien, upon the same being properly perfected. In this case the lien arises pursuant to the statute, and under and by virtue of the deed or transfer of the debtor's property, he being an insolvent, provided the creditors assail the same within the statutory period. To say that they should lose the right thus secured by taking the step necessary to secure or make the same effective would be an anomaly.

39. *In re Kirby-Dennis Co.*, 2 A. B. R. 402, 95 Fed. 116 (C. C. A. Wis., affirming 2 A. B. R. 218); *In re New England Breeders' Club*, 23 A. B. R. 689, 175 Fed. 501 (D. C. N. H.).

40. *In re Beck Prov. Co.*, 2 N. B. N. & R. 532 (Ref. Ohio); *Howard v. Cunniff*, 10 A. B. R. 74 (Ct. of Appeals, Mo.); *Crane Co. v. Smythe*, 11 A. B. R. 747, 87 N. Y. Supp. 917.

This view of the law has been steadily maintained by the bankruptcy courts under the present Bankruptcy Act."

However, in States where the filing of the affidavit comes too late if delayed until after creditors' rights have attached by levy of execution or attachment or otherwise, then, of course, it would be too late in bankruptcy, since the Amendment of 1910 to Bankr. Act, § 47 (a) (2), gives the trustee the rights of a creditor "armed with process."

§ 1156. Subcontractors' Liens.—The same rules would apply in most States to subcontractors' liens.⁴¹ But, owing to the phraseology of the statutes in some of the States, such liens have sometimes there been held not to arise and progress coincidently with the furnishing of the work or materials but to arise only upon the filing of the statutory affidavit or notice, not being merely perpetuated thereby. In such States the subcontractor has, in some decisions, been held to be a mere general creditor until he files his affidavit or notice, and the assignment of the contract by the head contractor would therefore defeat his rights. Therefore, in those States, if the head contractor is put into bankruptcy before the subcontractor has filed his affidavit or notice, the subcontractor may, by these holdings, lose his opportunity to get a lien. Such was the holding in the case of *In re Roeber*, 9 A. B. R. 303, 121 Fed. 449 (C. C. A. N. Y.), reversing 9 A. B. R. 778; itself reversed in *In re Grissler*, 13 A. B. R. 510, 136 Fed. 754 (C. C. A. N. Y.).⁴²

However, the Court of Appeals of New York State⁴³ held the same as the District Court, in this case, and it would therefore seem that the U. S. C. C. A. in 9 A. B. R. 303, is in error, the federal courts being bound to follow the decisions of the highest court of the State as to the validity of liens created by the State statutes. Subsequently the Circuit Court of Appeals corrected the error, in the case *In re Grissler*, 13 A. B. R. 510, 136 Fed. 754 (C. C. A. N. Y.).

In Pennsylvania the subcontractor acquires rights against the fund only by instituting suit and garnisheeing the owner; and therefore it is there held that the legal proceedings create the lien and do not simply enforce a lien already pre-existing.⁴⁴

41. *Fehling v. Goings*, 13 A. B. R. 154 (Court of Chancery, N. J.); *Crane Co. v. Smythe*, 11 A. B. R. 747, 94 App. Div. 53, 87 N. Y. Supp. 917; *In re Grissler*, 13 A. B. R. 508, 136 Fed. 754 (C. C. A. N. Y., rejecting its own former decision, *In re Roeber*, 9 A. B. R. 303, 121 Fed. 449); impliedly, *In re Cramond*, 17 A. B. R. 22 (D. C. N. Y.); *In re Huston*, 7 A. B. R. 92 (Ref. N. Y.).

Subcontractors' claims "allowed" only after deduction of fund appropri-

ated by attested accounts, *In re Grive*, 18 A. B. R. 737, 153 Fed. 597, 151 Fed. 711 (D. C. Conn.).

42. *Contra*, *In re Huston*, 7 A. B. R. 92 (Ref. N. Y.).

43. *Kane Co. v. Kenney*, 174 N. Y. 69, 9 A. B. R. 778, cited in *In re Grissler*, 13 A. B. R. 508, 136 Fed. 754 (C. C. A. N. Y.).

44. *Fairlamb v. Smedley Construction Co.*, 22 A. B. R. 824, 36 Pa. Super. Ct. 17.

§ 1157. **Liveryman's Liens.**—So, also, a liveryman's lien is not a lien created by legal proceedings nor dependent thereon, and is preserved in bankruptcy.⁴⁵

§ 1158. **Artisan's Liens.**—So, also, an artisan's lien is unaffected.⁴⁶

§ 1159. **Statutory Liens for Supplies.**—A lien given by statute for supplies furnished a manufacturing concern is unaffected by the Bankruptcy Act.⁴⁷ So, also, as to supplies furnished for motor vehicles.⁴⁸

§ 1160. **Landlord's Lien or Priority for Rent.**—A landlord's lien for rent or right to priority of payment on distribution is not impaired by the Bankruptcy Act.⁴⁹

It is not strictly speaking, a "lien by legal proceedings," and is not void under § 67 (f), though enforced by legal proceedings.⁵⁰

Henderson v. Mayer, 225 U. S. 631, 28 A. B. R. 387: "Similar rulings [see quotation of preceding portions of this decision at § 1155] have been made

45. In re Pratesi, 11 A. B. R. 319, 126 Fed. 588 (D. C. Del.); In re Mero, 12 A. B. R. 171, 128 Fed. 630 (D. C. Conn.).

46. In re Lowensohn, 4 A. B. R. 79 (D. C. N. Y.); Instance, In re Rich, 17 A. B. R. 893 (Ref. Ohio), taking from artisan's possession by deceit pending hearing on bankruptcy petition—lien still inheres. See ante, § 1145.

47. In re West Norfolk, 7 A. B. R. 648, 112 Fed. 767 (D. C. Va.); *Mott v. Wissler Mfg. Co.*, 14 A. B. R. 321, 135 Fed. 697 (C. C. A. Va.); In re Falls Shirt Mfg. Co., 3 A. B. R. 437 (D. C. Ky.); obiter, In re Lynn Camp Coal Co., 22 A. B. R. 60, 168 Fed. 998 (D. C. Ky.). See ante, § 1145.

Whether acceptance of chattel mortgage waives lien, In re Lynn Camp Coal Co., 22 A. B. R. 60, 168 Fed. 998 (D. C. Ky.).

48. Matter of McAllister-Newgord Co., 27 A. B. R. 459.

49. In re Belknap, 12 A. B. R. 326, 129 Fed. 646 (D. C. Pa.); In re Lines, 13 A. B. R. 318, 133 Fed. 803 (D. C. Pa.); In re Hoover, 7 A. B. R. 330 (D. C. Pa.); In re Mitchell, 8 A. B. R. 324, 116 Fed. 87 (D. C. Del.); In re Falls City Shirt Mfg. Co., 3 A. B. R. 437, 98 Fed. 592 (D. C. Ky.); impliedly, *Carriage Co. v. Solanas*, 6 A. B. R. 221 (D. C. La.); In re Byrne, 3 A. B. R. 268 (D. C. Iowa); impliedly, In re McIntyre, 16 A. B. R. 80 (D. C. W. Va.); *Wilson v. Penn. Trust Co.*, 8 A. B. R. 169, 114 Fed. 742 (C. C. A. Penn.); In re Goldstein, 2 A. B. R. 603 (Ref. Pa.); infer-

entially, In re Hayward, 12 A. B. R. 264, 130 Fed. 720 (D. C. Penn.); In re Gerson, 2 A. B. R. 170 (D. C. Penn.); In re West Side Paper Co., 20 A. B. R. 660, 162 Fed. 110 (C. C. A. Pa.); In re V. D. L. Co., 23 A. B. R. 643, 175 Fed. 635 (D. C. Ga.); instance, In re Hersey, 22 A. B. R. 860, 171 Fed. 998 (D. C. Iowa); *Henderson v. Mayer*, 28 A. B. R. 387, 225 U. S. 631; In re Meyer & Bleuler, 28 A. B. R. 17, 195 Fed. 653 (D. C. La.).

But compare, *Goldman v. Smith*, 2 A. B. R. 104 (Ref. Ky.), that claim of lien must be asserted in some manner within the statutory period notwithstanding intervening bankruptcy.

But compare, In re Duble, 9 A. B. R. 121, 117 Fed. 795 (D. C. Penn.), that the landlord may not distrain after tenant's adjudication as bankrupt but must rely wholly on priority under § 64 (b) (5).

And compare, In re Whealton Restaurant Co., 16 A. B. R. 294 (D. C. Penn.).

And compare, In re Jefferson, 2 A. B. R. 206, 93 Fed. 948 (D. C. Ky.), that the lien falls with the release of the contract obligation of the tenant.

Instance, where lien held on facts not to exist, *Des Moines Nat'l Bk. v. Council B. Sav.*, 18 A. B. R. 109, 150 Fed. 301 (C. C. A. Iowa).

50. See further, post, §§ 1437, 1444, 2204. Also, see In re Robinson & Smith, 18 A. B. R. 563, 154 Fed. 343 (C. C. A. Ill.); In re Seibold, 5 A. B. R. 358, 105 Fed. 910 (C. C. A. La.); *Plaut Tr. v. Gorham Mfg. Co.*, 23 A. B. R. 42, 174 Fed. 852 (D. C. N. Y.).

where the landlord has only a common-law right of distress. In *re West Side Paper Co.* (C. C. A. 3d Cir.), 20 A. B. R. 660, 162 Fed. 110, 89 C. C. A. 110. This is often referred to as a lien, but is only in the nature of security. 3 Black Com. 18. The pledge, or quasi-pledge, which the landlord is said to have, is, at most, only a power to seize chattels found on the rented premises. 'These he could take into possession and hold until the rent was paid. *Doe ex dem Gladney v. Deavors*, 11 Ga. 84. But before the distraint the landlord at common law has 'no lien on any particular portion of the goods and is only an ordinary creditor except that he has the right of distress by reason of which he may place himself in a better position.' *Sutton v. Reese*, 9 Jr. (N. S.) 456. It is true that prior to levy it covers no specific property, and attaches only to what is seized under the distress warrant issued to enforce the lien given by statute. But in this respect it is the full equivalent to a common-law distress, the lien of which is held not to be discharged by 67f. * * * The fact that the warrant could be levied upon property which had never been on the rented premises does not change the nature of the landlord's right, though it may increase the extent of his security.'

In *re West Side Paper Co.*, 20 A. B. R. 660, 162 Fed. 110 (C. C. A. Pa.): "Distress for rent in arrear, is one of the most ancient, as well as 'one of the most efficient of the landlord's remedies for the collection of rent.' It is in most of our States, as it was at common law, a right *sui generis*, belonging to the landlord whenever the relation of landlord and tenant existed. It appears to have been abolished in a few of the States, and in most of them its exercise has been regulated by statute. Its essential characteristics are, however, for the most part the same as existed at common law. In Pennsylvania, as at common law, the distress warrant issues directly from the landlord to his bailiff, who, if he happens to be a constable, is no less the agent and bailiff of the landlord than if he were a private person. The State law provides that, after the goods have been distrained, or levied upon, unless the same be replevied by the plaintiff within five days, the landlord may apply to the sheriff of the county, or to a constable, who is required to take proceedings for the sale of the said goods, or so much thereof as may be required for the satisfaction of the rent. In other respects, the right of the landlord remains for the most part as it was at common law. The right to distrain or levy upon all the goods upon the demised premises, whether those of the tenant or of a stranger, arises the moment the relation of landlord and tenant is established. It is a right in the nature of a lien, rather than a lien, until the goods are actually distrained under a landlord's warrant. It was originally in the nature of a property right in the *reditus* or return from the land, reserved to the landlord. No suit or proceeding at law, whether in personam or in rem, in the proper sense of those words, was necessary for the assertion of this right. It belongs to that small category of personal rights, the assertion of which has always been independent of legal procedure; of which the right to abate a nuisance, under certain circumstances, and the right to distrain cattle damage feasant, are examples. While there is no specific lien, except on the goods actually distrained under the landlord's warrant, all the goods on the demised premises are to be considered as being under a quasi pledge, which gives superiority to the specific lien established by the distraint. Such a lien is in no sense 'obtained through legal proceedings.' Nor is it within the spirit of the bankrupt law in this regard, as evidenced by other provisions thereof, as well as that of 67f, above quoted."

In *re Burns*, 23 A. B. R. 640, 175 Fed. 633 (D. C. Ga.): "See particularly the opinion of Circuit Judge Grosscup, In *re Robinson & Smith*, 18 Am. B. R. 503, 154 Fed. 343, speaking for the Circuit Court of Appeals for the Seventh

Circuit, when he held that the provision of the bankruptcy law on which the trustee here relies 'relates only to those actions of proceedings taken by creditors who, having no existing lien or right of lien, resting in existing contract, entered into in good faith, seek to obtain a preference by being first in the race of diligence, and such provisions do not affect that lien obtained by a landlord by the levy of a distress warrant for rent.' This case is precisely in point, and long postdates any adverse holding. 'The right of the landlord is one upon which every permanent hope of general prosperity must depend. Our legislature, in the several statutes set forth in the various sections of the Code of Georgia, have made very clear the policy of the State on this subject. Section after section reiterates not only the right of the landlord to a general lien, but they also give a special lien upon the crops made on the land. The general lien attaches to all of the property of the debtor liable to levy and sale. It is true that this lien attaches from the date of the levy, but that does not mean that the right of the landlord to the general lien, or to the special lien, is created by levy. The right exists by virtue of the statute.

* * * But the State law has created the general right, and as well the special right, and the lien of the landlord thus created is one of those debts having priority by the law of the State, which under the express provisions of the Bankruptcy Act * * *, must be paid from the assets of the bankrupt, provided the lien has attached, before the general creditors can participate therein. It follows, in my judgment, that the bankruptcy of the tenant does not defeat this lien of highest dignity except the lien of taxes."

But this subject is complicated by the fact that landlords are frequently also given priority by State law, upon distribution of an insolvent's estate, regardless of lien, and that this priority is preserved in bankruptcy by § 64 (b) (5). Therefore, these latter cases come with equal propriety both under the subject of the preservation of State priorities under Bankruptcy Distribution, and under the subject of the preservation of liens.⁵¹

§ 1161. Mechanics' Liens, etc., Valid Though Affidavit or Stop Notice Not Filed Till after Bankruptcy of Owner, etc.—A mechanic's or materialman's lien may be valid, even if the affidavit is not filed until after bankruptcy of the owner of the building.⁵²

So, also, a lien given by statute for supplies furnished to a manufacturing or mining concern necessary to its operation, may be valid even if the statutory memorandum is not filed until after the bankruptcy, if it be filed within the statutory limitation of time.⁵³

51. Also, see post, subjects of "Distribution," and "Claims Entitled to Priority under State Laws," § 2204.

52. See note to *In re Kirby-Dennis Co.*, 2 A. B. R. 218 (D. C. Wis.); impliedly, *In re Beck Prov. Co.*, 2 N. B. N. & R. 532 (Ref. Ohio); *In re Lillingston Lumber Co.*, 13 A. B. R. 153, 132 Fed. 886 (D. C. N. Car.); *In re Georgia Handle Co.*, 6 A. B. R. 472, 109 Fed. 632 (C. C. A. Ga.); *Kane Co. v. Kinney*, 9 A. B. R. 778, 174 N. Y. 69, 66

N. E. 619, followed in *In re Grissler*, 13 A. B. R. 509, 136 Fed. 754 (C. C. A. N. Y.). See ante, this subdiv., § 1155. But compare, analogously, peculiar decision *In re Epstein*, 19 A. B. R. 89, 156 Fed. 42 (C. C. A. Colo.), quoted at § 1806½; compare, *In re Clark Coal & Coke Co.*, 23 A. B. R. 273, 173 Fed. 658, 176 Fed. 955 (D. C. Pa.).

53. *Mott v. Wissler Mfg. Co.*, 14 A. B. R. 321, 135 Fed. 697 (C. C. A. Va.).

To same effect, *In re West Norfolk Lumber Co.*, 7 A. B. R. 648, 112 Fed. 767 (D. C. Va.): "The time of furnishing the supplies is the period as of which the materialman is given a right of lien. The right to claim the lien arises under this section and may be enforced at any time after the supplies are furnished; but may be lost by failure to comply with some provisions of the Act giving the right. The only requirement is that the lien shall be filed within the 90 days after the last item of the bill becomes due and payable. If the claim is filed within that time, the lien secured relates to the time the supplies were furnished."

Likewise, the subcontractor may serve his "stop" notice or file his affidavit after the bankruptcy of the owner;⁵⁴ or after the bankruptcy of the head contractor.⁵⁵

§ 1162. Failure to Perfect Lien in Statutory Form Invalidates.—Failure to perfect the lien according to the statutory formalities invalidates it.⁵⁶

In re Kerbey-Dennis Co., 2 A. B. R. 402, 95 Fed. 166 (C. C. A. Wis., affirming 2 A. B. R. 218, 94 Fed. 818): "The apparent inequity, in now denying equity, results, however, not from the Bankruptcy Act, but from their own omission to comply with the requirements of the local law. Both of these classes of laborers had liens upon the product upon which their labor was expended. The one class preserved their liens by proper proceedings, which the statute giving the lien rendered imperative for its continuance. The other class omitted so to do, and, therefore, by force of the statute which created the right, the lien is gone forever."

Grainger & Co. v. Riley (In re Globe Printing Co.), 28 A. B. R. 114, 201 Fed. 901 (C. C. A. Ky.): "The statute authorizes a lien in favor of mechanics, laborers and materialmen, and provides that no person shall acquire this lien, unless he shall notify in writing the owner of the property to be held liable or his authorized agent, immediately after the last item of material or labor is furnished, of his intention to hold the property liable and the amount for which he claimed a lien. Nothing is left to inference or conjecture. A compliance with this provision is, as we think, *conditio sine qua non*. A lien, such as is sought here, for labor performed or material furnished is unknown to the common law, and is a purely statutory one. That there must be a substantial compliance with the terms of such statute is everywhere maintained and upon the conditions provided or in the act giving the lien."

In re Franklin, 18 A. B. R. 220, 151 Fed. 642 (D. C. N. Car.): "Before a creditor can claim a lien given by a State statute he must comply with the statute and perfect his lien. It is only after so perfected that they are protected by the court of bankruptcy or by any other court."

⁵⁴ *In re Grissler*, 13 A. B. R. 508, 136 Fed. 754 (C. C. A. N. Y., reversing its own former ruling in *In re Roeber*, 9 A. B. R. 303, 121 Fed. 449); inferentially, *Fehling v. Goings*, 13 A. B. R. 134 (N. J. Chan.); *In re Lillington Lumber Co.*, 13 A. B. R. 153, 132 Fed. 886 (D. C. N. Car.).

⁵⁵ *Crane Co. v. Smythe*, 11 A. B. R. 747, 87 N. Y. Supp. 917. In this case it was, in substance, held, that the ad-

judication in bankruptcy of a building contractor did not cut off the right of a materialman to file and enforce his lien for materials used in the building.

⁵⁶ *In re Cramond*, 17 A. B. R. 34 (D. C. N. Y.).

Verbal Notice to Owner under Ohio Law.—Notice to the owner of the filing of the lien affidavit may be verbal. See *In re Boner*, 26 A. B. R. 321, 189 Fed. 93 (D. C. Ohio).

§ 1163. But Where Perfecting Dependent on Legal Proceedings, Bankruptcy May Dispense with Same.—But where the perfecting or maintaining of a lien is by state statute made to depend upon the taking of certain legal proceedings within a specified time, the lien is absolved from such condition by the bankruptcy itself, the property thereby being already in custodia legis such that interference with it would be contempt.⁵⁷ Or perhaps the Bankruptcy Court would permit such proceedings to be taken with limitation of their effect, in analogy to the rule prevailing in regard to exempt property and to perfecting rights against a surety on a bankrupt's appeal bond.⁵⁸

§ 1164. Consent to Payment of Fund into Bankruptcy Court.—Where all parties in lien cases consent that the owner may pay the fund into the bankruptcy court, the litigation may be there carried on.⁵⁹

§ 1165. Without Consent, State Court Proper Forum, Where Contractor or Subcontractor Bankrupt.—Without consent of the parties, the state court is the proper forum, where it is not the owner but the contractor or subcontractor who is the bankrupt, and where third parties claim interests; ⁶⁰ likewise, where the bankrupt was owner but sold the property before the bankruptcy, the purchaser retaining part of the purchase price to take care of liens that might be filed.⁶¹

The rule would be different were it specific property that was thus placed by a stake holder in the custody of the bankruptcy court without the consent of the other parties. In that event the actual possession of the property would carry with it jurisdiction to adjudicate the rights of all persons claiming interests therein, whether such persons would consent to the jurisdiction or not. But the subject of subcontractors' liens is a debt—the owners' debt to the head contractor, which they have sought to appropriate by filing their subcontractors' claims; and, no matter if the owner pay an equivalent sum of money into the bankruptcy registry, he cannot thereby discharge his debt without the subcontractors' consent, and the subcontractors may still sue him for the debt garnisheed by their statutory affidavits, notwithstanding. The bankruptcy court is not an appropriate forum for suing the owner for a mere debt, jurisdiction to recover debts—unless they be the money expression of the value of property belonging to the estate—not existing in the bankruptcy courts, even by the Amendment of 1903.⁶²

⁵⁷. In re Falls City Shirt Mfg. Co., 3 A. B. R. 437, 98 Fed. 592 (D. C. Ky.).

⁵⁸. Compare, §§ 1102, 1104, et seq; also §§ 2711, 2712. Compare, also, the opinions of the various courts on the subject of rents of mortgaged premises of the bankrupt accruing after adjudication. § 656, et seq.

⁵⁹. Impliedly, In re Huston, 7 A. B. R. 92 (Ref. N. Y.).

⁶⁰. Obiter, impliedly, In re Adamo,

18 A. B. R. 181, 151 Fed. 716 (D. C. N. Y.); impliedly, In re Grissler, 13 A. B. R. 508, 136 Fed. 754 (C. C. A. N. Y.); apparently contra, In re Hobbs, 16 A. B. R. 544 (D. C. W. Va.). See post, "Conflict of Jurisdiction."

⁶¹. In re Greater American Exposition, 4 A. B. R. 486, 102 Fed. 986 (C. C. A. Neb.).

⁶². See post, "Jurisdiction over Adverse Claimants," § 1682; also, § 1697.

SUBDIVISION "C."

DOWER RIGHTS, CURTESY RIGHTS AND WIDOW'S AND CHILDREN'S DISTRIBUTIVE SHARE.

§ 1166. **Inchoate Dower Right Unimpaired.**—The inchoate right of dower is unimpaired and the trustee takes the property subject to the right becoming consummate through the bankrupt's death.⁶³

§ 1166¹/₄. **Except Where Dower Not Good against Levying or Judgment Creditors.**—But inchoate dower is cut off by the husband's bankruptcy where it would be cut off under the state law as against a levying creditor; and it has been held in Pennsylvania that, since the Amendment of 1910 to the Bankruptcy Act, § 47a (2), confers upon the trustee the attributes of a creditor "armed with process," dower right is barred, since in that State a sale on execution bars dower in the execution debtor's real estate.⁶⁴

In *re Codori*, 30 A. B. R. 453, 207 Fed. 784 (D. C. Pa.): "Whether the right to dower under the order if sold accordingly, would have been extinguished depends entirely upon the amendment of § 47a(2) of the Bankruptcy Act, since before a sale would not have so operated. *Lazier v. Porter*, 109 U. S. 84; In *re Shaeffer* (D. C., Pa.), 5 Am. B. R. 248, 105 Fed. 352. By the provisions of § 70, subdivision 5, the trustee is invested with the bankrupt's title to all property which he, prior to the filing of the petition, could have transferred, or by judicial process might have been sold for him. And as to such property the trustee by § 47a(2) as amended, by the Act of June 25, 1910, 'shall be deemed vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceeding thereon.' The trustee, therefore, as has often been decided, concerning such real estate of the bankrupt in his possession, is in the position of a lien creditor. The amendment had the effect of vesting in the trustee the enlarged rights, remedies and powers of a judgment or other creditor having a lien upon the bankrupt's real estate (*Bank of North America v. Penna. Motor Car Co.*, 235 Pa. 194), enabling him to sell such real estate acquitted and discharged of the inchoate right of the widow's dower, to the same effect as by a sheriff's sale after levy on proper writ of execution.

"In Pennsylvania the widow's right to dower in her husband's real estate has not been favored so as to exclude the just demands upon it for his debts. She is entitled to dower only in what remains of her husband's estate after payment of debts. His land has always been held as an asset or chattel for the payment of his debts; and the sale of his land on judgment, mortgage or other lien whatever has been held to bar the wife's right of dower in such

63. *Thomas v. Woods*, 23 A. B. R. 132, 173 Fed. 585 (C. C. A. Kans.), quoted at § 1166¹/₂; In *re Slack*, 7 A. B. R. 121, 111 Fed. 523 (D. C. Vt.); impliedly, In *re Acretelli*, 21 A. B. R. 537, 173 Fed. 121 (D. C. N. Y.). Compare to same effect, inferentially, In *re Shaeffer*, 5 A. B. R. 248, 105 Fed. 352 (D. C. Pa.); obiter, *Bush v.*

Export Storage Co., 14 A. B. R. 143, 136 Fed. 918 (U. S. C. C. Tenn.).

Dower where there is a purchase money mortgage, computable on surplus only, in Ohio, In *re Hays*, 24 A. B. R. 669, 181 Fed. 674 (C. C. A. Ohio).

64. In *re Freedman*, 29 A. B. R. 135, (Ref. Pa.); In *re Freedman*, 31 A. B. R. 53 (D. C. Pa.).

land. *Director of the Poor v. Royer*, 43 Pa. 146. Hence the order to sell free and discharged of liens by the enlarged authority conferred by the amendment placing the trustee into the position of a lien creditor contemplated the discharge of the widow's inchoate right of dower and the trustee had no authority to sell otherwise. To have done so beyond doubt operated to the prejudice of the bankrupt's creditors, since it is well understood that real estate is not as desirable with as without such interest as the trustee attempted to reserve."

§ 1166½. Dower in Lands Located in Another State.—From the wording of the statute, it might seem that where the bankrupt owns real estate located in another State, and dies, his widow is entitled to such dower rights as would belong to her in the State of the bankrupt's residence.⁶⁵

Such a construction, however, might lead to the giving of greater or perhaps less dower to the widow than she would be entitled to under the laws of the State where the land was actually located; and it is altogether likely that the proviso of § 8, "That in case of death the widow and children shall be entitled to all rights of dower and allowance fixed by the laws of the State of the bankrupt's residence," should be read as if the clause "fixed by the laws of the State of the bankrupt's residence" modified simply "allowance" and not also "dower;" by this construction the right of dower being left in each State in precisely the condition the State law intended.

Thomas v. Woods, 23 A. B. R. 132, 173 Fed. 585 (C. C. A. Kans.): "It is next urged that the right of dower belongs in the same class as the right of exemptions and homesteads, which are confined by § 6 of the Bankruptcy Act to the State of the bankrupt's domicile. Their similitude is very slight. Both are in a general way for the protection of the family. There, however, their likeness ceases. The homestead and exemptions are a part of the bankrupt's estate. They are both primarily to be claimed by him and set off to him. Their selection from his estate arises at the time when that estate is to be appropriated to the payment of the claims of his creditors. Dower, on the other hand, is no part of the bankrupt's estate. The wife derives no right from him either by grant or contract. As the Supreme Court says in *Randall v. Krieger*, 23 Wall. 137, 148: 'It is wholly given by law.' Congress has plenary power over the subject of exemptions, because they are part of the bankrupt's estate. It may, as in the present law, adopt the exemption laws of the several States, or it may, as in the Act of 1867 * * *, adopt local laws in part, and supplement these with a schedule of its own. Its power to deal with the subject, however, arises out of the fact that exemptions are a part of the bankrupt's estate. This consideration shows that the right of dower does not belong in the same class. Again, the right of dower has nothing to do with the insolvency of the husband. It arises from time to time during the marriage relation as the husband acquires real property. If the wife has not released her right of dower, it is as much her own private, absolute property as if she had acquired it by purchase. That estate can no more be transferred to

⁶⁵. *Bank v. Act*, § 8; *Hurley v. Devlin*, 18 A. B. R. 627, 151 Fed. 919 (D. C. Kans.), overruled by *Thomas v. Woods*, 23 A. B. R. 132, 173 Fed. 585

(C. C. A.); contra, *Thomas v. Woods*, 23 A. B. R. 132, 173 Fed. 585 (C. C. A. Kans.), quoted at § 1166½.

her husband's creditors than any other portion of her separate estate. At the present time in the United States, the wife, as to her property rights, is a third person, and her estate is no more affected by the insolvency of her husband than is the property of other third parties. In our judgment it would be beyond the constitutional power of Congress to provide that in case of bankruptcy the dower rights of the bankrupt's wife, as defined by laws of the several States, ceased, and the real property owned by him passed to his trustee in bankruptcy discharged from such right of dower. Bankruptcy can only deal with what in law belongs to the bankrupt. It may annul his acts and the acts of his creditors which interfere with the just enforcement of its provisions. It cannot, however annul an act of the legislature of a State which previous to the statute of bankruptcy had vested an estate in the wife of the bankrupt. Its whole field of operation is circumscribed to getting in the estate which under the law belongs to the bankrupt, and distributing the same to his creditors. It cannot reach out and take property which under the laws belongs to the wife, and apply it to the payment of the bankrupt's debts, any more than it could seize that portion of her property which she acquired by purchase or devise. Again, it does not follow that because the right of homestead and exemptions is confined in most of the States to the domicile of the claimant, such a restriction would be appropriate in regard to dower. Dower is not measured in value or quantity as homesteads or exemptions are. The amount of it is dependent solely upon the amount of real property of which the husband is seized. * * * The proviso deals with two classes of rights: First, the widow's right of dower in real property; second, the allowances to the family out of the personal estate. This second class of rights is necessarily fixed by the laws of the State of the bankrupt's residence, for general rights in personal property follow the person of the owner and are determined by the laws of the State of his residence. The framer of the proviso used, in its last clause, language which was entirely appropriate to the allowances, and in part appropriate as to the right of dower. Having in mind several classes of rights, he made the not uncommon mistake of using language which was not quite comprehensive enough to cover all those rights under all conditions. If the proviso was a grant of rights, there would be reason in restricting the rights to its language; but, being intended to protect existing rights, it ought not to be given an interpretation which would destroy any part of those rights."

It has been held that the bankruptcy court wherein the adjudication of bankruptcy was had may determine the rights of dower in land located in another State, in the custody of the trustee there.

Hurley v. Devlin, 18 A. B. R. 627, 151 Fed. 919 (D. C. Kans., sustained on this point, though reversed on other points, by *Thomas v. Woods*, post): "The ultimate question for determination, therefore, is, shall the trustees of the estate being administered in this court at the suit of the widow be compelled to appear in the State courts of foreign states to defend their interests, or supposed interests in the estate, when at the time such suits were brought they were in the actual possession of the property in the custody of this court, in the due process of administration. * * * While the act itself nowhere provides in what court or by what procedure the widow's rights to dower and the allowance to the widow and children provided for by § 8 thereof is to be determined and set apart, yet the above-quoted provisions clearly stake out, define, and limit the rights of the widow and the creditors of the deceased bankrupt as represented by the trus-

tees in the bankrupt estate. Hence, it is clear, in whatever court jurisdiction of the controversy resides, the rights of the parties are governed, controlled, and must be measured by the Bankrupt Act, and not by the laws of the particular State in which the property is situate, except in so far only as such laws are adopted and preserved by the act for the determination of such rights. As has been seen, this was the State of the residence of the bankrupt before the commencement of the bankruptcy proceedings. For this reason jurisdiction was conferred upon this court by the Bankrupt Act for the purpose of entertaining the voluntary petition of the debtor to be adjudged a bankrupt, to take possession of his property through its appropriate officers, wherever situate, to conserve the estate, and to determine the rights of the respective creditors, and all others therein, and through its trustee or trustees to set apart all exemptions to the bankrupt and to pass title to nonexempt property to the purchasers thereof from the trustees in the settlement of the sequestered estate. As has been further seen before the death of the bankrupt, while the widow's right of courtesy or dower in the lands of her husband remained inchoate, and for that reason afforded her no right of suit or action for its ascertainment and allowance, the trustees of the estate reduced the same to their actual possession, and were proceeding with the administration of the estate in this court in conformity with the provisions of the act, when the contingency giving her the right of action for her dower happened, and when the suits were brought by her in the State courts of foreign States. This court having assumed jurisdiction of the administration of this bankrupt estate, and having through its receivers taken actual possession of the property in which the widow, by the happening of the subsequent event of the death of her husband, acquired the interest she now asserts (an interest in and right to a portion of such property), I am of the opinion the determination of the controversy involving such right is drawn to and must be asserted in this court having jurisdiction of the administration of the estate and the custody of the property; that this jurisdiction, of necessity, is exclusive, and that the widow may, if she is so advised by her solicitors, exhibit her bill against the trustees and all parties in interest in said property, and all property in which she claims to be endowed out of her husband's estate to this court, and that this court, has full, ample, and exclusive jurisdiction to cause all such parties to be brought before it and to make complete determination of the rights of all parties." See § 1706½.

Or otherwise in the custody of the bankruptcy court, as, for instance, in the custody of the bankrupt at the date of the filing of the bankruptcy petition.

Thomas v. Woods, 23 A. B. R. 132, 173 Fed. 585 (C. C. A. Kans., reversing on other grounds and affirming on this ground *Hurley v. Devlin*, *supra*): "The objection of the appellant that the trial court was without jurisdiction of the property, because it was not situated in the district of Kansas, has no merit. Upon the filing of a petition in bankruptcy, all property held by or for the bankrupt is brought within the custody of the court of bankruptcy, and, upon adjudication, that court is vested with jurisdiction to determine all liens and interests affecting it. This jurisdiction is coextensive with the United States."

It is questionable, however, whether the bankruptcy court has such jurisdiction to adjudicate titles to real estate in other States. Though the act is a "uniform law," yet that does not give the bankruptcy court extra-territorial jurisdiction; and in matters of title to real estate jurisdiction has always been particularly confined to land within the district, though indirectly land elsewhere may be affected by the exercise of control over

parties interested therein who may be found in the district. Were it not so, in the course of years, the devolution of title to real estate from one to another, with all the vicissitudes of the successive owners involved, would complicate the search of records intolerably, sometimes resulting in the search of titles in many different States, each State a one time State of the residence of some bankrupt owner of the land. Doubtless, ancillary bankruptcy proceedings might be instituted for such purpose in the district wherein the land is located.

§ 1166³. Release of Dower in Preferential or Fraudulent Mortgage.—A release of dower is a mere incident to the transfer itself and falls with the fall of the transfer, so that such a release by a bankrupt's wife does not remain available to a mortgagee upon the avoidance of the mortgage itself as being preferential or fraudulent against the bankrupt's creditors.⁶⁷

§ 1167. Widow's and Children's Allowances.—The widow's and children's allowances are a charge upon the property coming into the bankruptcy court if the bankrupt dies after the petition is filed and before adjudication.⁶⁸ But if he die after adjudication, the widow and children have no right to allowance out of the bankrupt assets.⁶⁹

SUBDIVISION "D."

SELLER'S RIGHT OF STOPPAGE IN TRANSITU AND TO RESCIND SALE.

§ 1168. Right of Stoppage in Transitu Unimpaired.—The seller's right of stoppage in transitu is unimpaired;⁷⁰ likewise his right to retain possession, in case of the buyer's insolvency, before transit begins.⁷¹

In re Darlington, 20 A. B. R. 800, 163 Fed. 389 (D. C. N. Y.): "The doctrine of stoppage in transitu can only be invoked where insolvency exists, and except for the provisions of the bankruptcy statutes of 1867 and 1898, the administration of insolvent estates in the United States has been under the various assignment acts of the different States. Such laws relating to assignments and the general doctrines of insolvency, recognize preferences and preferential payments. But both the Bankruptcy Act of 1867 and that of 1898 make preferential payments within a certain period voidable, and provide against the recognition of preferences in the administration of the bankrupt estate. The theory of the present

⁶⁷. In re Lingafelter, 24 A. B. R. 656, 181 Fed. 24 (C. C. A. Ohio).

⁶⁸. Bankr. Act, § 8.

⁶⁹. In re McKenzie, 15 A. B. R. 679, 142 Fed. 383 (C. C. A. Ark.); compare, In re Seabolt, 8 A. B. R. 57, 113 Fed. 766 (D. C. N. Car.); contra, In re Parschen, 9 A. B. R. 389, 119 Fed. 976 (D. C. Ohio); contra, In re Newton, 10 A. B. R. 345, 122 Fed. 103 (D. C. Conn.); contra, In re Dicks, 28 A. B. R. 845, 198 Fed. 293 (D. C. Ga.); compare, In re Slack, 7 A. B. R. 121, 111 Fed. 523 (D. C. Vt.). See ante, "Death of Bankrupt

before Adjudication but after Petition Filed," § 99.

⁷⁰. In re Burke & Co., 15 A. B. R. 495 (D. C. Pa.); obiter, In re Portuondo Co., 14 A. B. R. 337, 135 Fed. 592 (D. C. Pa.).

Compare on facts, but not placed on this ground, *Pridmore v. Puffers Mfg. Co.*, 20 A. B. R. 851, 163 Fed. 496 (C. C. A. S. C.). Compare effect of Amendment of 1910, ante, § 1144.

⁷¹. In re Portuondo Co., 14 A. B. R. 337, 135 Fed. 592 (D. C. Penn.).

bankruptcy law would seem to be utterly hostile to the idea of returning to a creditor, goods as to which title but not actual possession had passed to the bankrupt, and thus securing to the creditor who stops the goods payment in full, as against partial dividends to other creditors. But at the time the bankruptcy law of 1867, and the bankruptcy law of 1898, were passed, the doctrine of stoppage in transitu was well known in the courts and in the general body of the law. The application of the doctrine of stoppage in transitu, since the passage of the Bankruptcy Act, and its recognition by the courts, indicates that it cannot be inferred from the bankruptcy statute that a principal of law, so recognized by the courts as to have become a legal right, was wiped out and intended to be disregarded, when no express evidence of that intent was set forth in the text of the law. For the sake of consistency, and in order to carry out the principle of the bankruptcy statute, that the filing of a petition and the appointment of a receiver is notice to the world and creates an inchoate title which cannot be disregarded by those who have in their possession any part of the bankrupt estate, as indicated in the *Mulder* case, *supra*, the doctrine of stoppage in transitu might have been excluded, if it had seemed wise to those framing the law so to do. But, as has been said, the trend of decision and the language of the statutes seem to indicate that no change in the doctrine of stoppage in transitu was made by either of the Bankruptcy Acts of the United States, and the present case must depend upon the determination of the issue involved, according to the principle of that doctrine as set forth by decisions."

A claim presented against the estate by one who wrongfully stopped goods in transit, may be reduced to the extent of the loss caused by his action.⁷²

The right of stoppage in transitu has been lost if the goods reach the actual possession of the trustee at the designated terminus; and the same rule has been enunciated as to the possession of the receiver, even though the goods were shipped after the consignee had gone into bankruptcy.⁷³

In *re Allen*, 24 A. B. R. 574, 178 Fed. 879 (D. C. Pa.): "In the meantime, however, the receiver, being informed that there were some goods at the freight house which belonged to the bankrupt, went and got them, paying the freight charges and having the goods hauled to the bankrupt's store by a drayman. Until there was an actual delivery the right of the petitioners to stop and reclaim the goods was unquestionable. But not afterwards. It was too late, once the receiver representing the estate had taken possession of them."

Seizure before the goods have reached their destination will not, however, end the right of stoppage in transitu.

§ 1169. Right to Rescind for Fraud Unaffected.—The seller's right to rescind a sale for fraudulent misrepresentations, etc., is unaffected.⁷⁴

⁷² In *re W. A. Patterson Co.*, 25 A. B. R. 855, 186 Fed. 629 (C. C. A.).

⁷³ Compare post, § 1881.

⁷⁴ See post, "Reclamation Proceedings," § 1879, et seq. In *re Hamilton Furniture & Carpet Co.*, 9 A. B. R. 65 (D. C. Ind.); In *re Marco Gany*, 4 A. B. R. 576 (D. C. N. Y.); In *re Weil*, 7 A. B. R. 90, 111 Fed. 897 (D. C. N.

Y.); In *re O'Connor*, 9 A. B. R. 18, 114 Fed. 777 (D. C. Ga.); In *re Patterson & Co.*, 10 A. B. R. 748, 125 Fed. 562 (D. C. Tex.); impliedly, In *re Russell & Birkett*, 5 A. B. R. 608 (Ref. N. Y.); *Haywood v. Pittsburg Industrial Iron Works*, 19 A. B. R. 780, 163 Fed. 799 (D. C. Pa.).

Instances where right of rescission

In all these instances, the seller's substantive rights are unimpaired and he may retake the property if he makes out a case, although he may be obliged to seek his forum in the bankruptcy court itself rather than in the State Courts;⁷⁵ likewise, the seller may retain the property, if he has on these grounds, before the bankruptcy, already rescinded the sale and obtained possession.⁷⁶

SUBDIVISION "E."

SET-OFF AND COUNTERCLAIM.

§ 1170. Right of Set-Off and Counterclaim Unimpaired.—The right of set-off and counterclaim is as valid against the trustee as it would have been against the debtor had he not gone into bankruptcy,⁷⁷ and the trustee takes choses in action and other property subject thereto.⁷⁸

denied: Failure to make out case because of seller's admission or proof that the seller would have sold the goods anyway, the fraudulent misstatement being denied by the bankrupt. In *re Davis*, 7 A. B. R. 276, 112 Fed. 294 (D. C. N. Y.).

No tender back of the consideration received. In *re Murphy Barbee Shoe Co.*, 11 A. B. R. 434 (Ref. Mo.).

No reliance on the false statement. In *re Epstein*, 6 A. B. R. 60, 109 Fed. 878 (D. C. Ark.); In *re Roalswick*, 6 A. B. R. 752, 110 Fed. 639 (D. C. Mont.). Whether affected by Amendment of 1910, see ante, § 1144.

75. *Bloomington v. Empire Rubber Mfg. Co.*, 8 A. B. R. 74, 114 Fed. 1016 (D. C. N. Y.).

76. *Impliedly, Lumber Co. v. Taylor*, 14 A. B. R. 231, 137 Fed. 321 (C. C. A. Pa.): And if the property has been sold by the bankruptcy court after he filed his petition claiming them he may recover the proceeds of the sale.

In *re Weil*, 7 A. B. R. 90, 111 Fed. 897 (D. C. N. Y.): Should he not be entitled to recover their entire value if the sale was made without his consent?

But if the goods have become component parts of a structure not separable therefrom without manifest injury to the whole, the right to retake the specific goods is lost. *Lumber Co. v. Taylor*, 14 A. B. R. 231, 137 Fed. 321, 137 Fed. 321 (C. C. A. Pa.): "The lumber, purchased of defendant, having only entered into the partial construction of the barges, no right of title thereto could be acquired by defendant's rescission of the sale for fraud."

Pleading and Practice in Asserting Such Right.—See post, "Reclamation

of Goods on Rescission of Sales for Fraudulent Misrepresentations," § 1879.

See § 805¼ for claims against estate on rescission of contracts to purchase stock.

77. In *re Searles*, 29 A. B. R. 635, 200 Fed. 893 (D. C. N. Y.).

78. Bankr. Acts, § 68: "In all cases of mutual debts or mutual credits between the estate of a bankrupt and a creditor the account shall be stated and one debt shall be set off against the other, and the balance only shall be * * * allowed or paid."

Stich v. Berman, 15 A. B. R. 467 (Sup. Ct. N. Y. App. Div.); *Norfolk & W. Ry. Co. v. Graham*, 16 A. B. R. 615, 145 Fed. 610 (C. C. A. W. Va.); *Whittlesey v. Becker & Co.*, 25 A. B. R. 672 (Sup. Ct. N. Y.).

Instance, *McDonald v. Clearwater Ry. Co.*, 21 A. B. R. 182, 164 Fed. 1007 (U. S. C. Idaho); *Walthers v. Williams Mercantile Co.*, 22 A. B. R. 328, 169 Fed. 270 (C. C. A. Mich.), wherein a bailor of stock of goods and business which has been delivered to a firm to operate upon condition that the bailee firm should keep it replenished and pay certain percentages to the bailor for the use, was held entitled, on repossessing the business, to off-set the unpaid commissions and other charges against the increased value of the business; *Taylor v. Nichols*, 23 A. B. R. 306, 134 App. Div. (N. Y.) 783; In *re Harper*, 23 A. B. R. 918, 175 Fed. 412 (D. C. N. Y.). See ante, § 818½; post, § 1203. Whether affected by Amendment of 1910, see ante, § 1144.

Off-set refused because delayed until after bankruptcy petition filed. *Moore v. Third Nat'l Bk.*, 24 A. B. R. 568 (Pa. Superior Court).

A sum paid to a landlord for an

§ 1171. Which Governs: Law of State, United States, or of Forum.—But, except as the Bankruptcy Act itself amplifies or modifies the right, the exercise of the right, it has been held, will be subject to the rules regarding set-offs prevailing in the federal courts of the district rather than to those prevailing in the state courts.

Trustee v. Mercantile Nat'l Bk., 14 A. B. R. 128, 182 N. Y. 264 (N. Y. Court of Appeals): "As the bankrupt law operates throughout the whole country, the construction to be given to it must necessarily be uniform throughout all the States, not varying with the local law. Therefore, in construing it we should be governed by the law of set-offs as it prevails in the Federal Courts and not in our own."

But ought not the rule rather be, that, except as the Bankruptcy Act itself modifies or amplifies it, the rule of the court, State or Federal, wherein the remedy is applied should prevail?

§ 1171½. Mutual Demands Must Have Existed.—Mutual demands must have existed.⁷⁹

In re Northrup, 20 A. B. R. 86, 159 Fed. 686 (C. C. A. N. Y.): "The District Court also reached the conclusion that the Syracuse Bank remitted the proceeds of its collections to the Central Bank through a mistake of fact. This conclusion is apparently based upon the assumption that, had the Syracuse Bank been advised of the collection of the Paul draft, it would have set off the accounts. But it does not appear that the Syracuse Bank had any right to make such offset. On the contrary, it seems clear that it had no such right. The bankrupts undoubtedly acted wrongfully in failing to give notice of the collection of the Paul draft. But this was a matter outside the obligation of the Syracuse Bank to remit for what it had collected."

It has been held that money remitted to a creditor for a specific purpose cannot, by application against the debtor's will to another purpose, be converted into a debt so that it may come within the rules of offset of mutual debts or demands.

[1867] *Stewart v. Hopkins*, 30 Ohio St. 541: "The money was remitted to the plaintiffs for a specific purpose. It was not intended the title thereto should pass to them for another purpose. The plaintiffs were not, therefore, authorized, by crediting it on account, to convert it into a mere debt. Nor was it money remitted to be used, or held in trust, in any manner to result in a debt of the plaintiffs to Hopkins or Hopkins & Co. Strictly speaking, then, it could not be classed as among the "mutual debts or mutual credits between the parties," authorized by the twentieth section of the bankrupt law, to be set-off against each other; for that section was not intended to change or enlarge the law of set-off beyond what the principles of legal or equitable set-off previously authorized. *Sawyer v. Hoag*, 17 Wall. 610. Ordinarily that does not become a debt which

extension of the term may be set off against a claim for rent. *In re Abrams*, 29 A. B. R. 590, 200 Fed. 1005 (D. C. Iowa).

The origin and history of this provision is discussed by Chief Justice Holmes of Massachusetts in *Mor-*

gan v. Wordell, 6 A. B. R. 167, 59 N. E. 1037 (Mass.). Compare, also, discussion in *In re Becher Bros.*, 15 A. B. R. 228, 139 Fed. 366 (D. C. Penn.).

^{79.} *In re T. M. Leshner & Son*, 25 A. B. R. 218, 176 Fed. 650 (D. C. Pa.).

was not intended as such, nor a credit that was not in contemplation of the parties to become a credit in the nature of a debt. *Waterman on Set-Off*, §§ 148 and 153."

§ 1172. And Must Have Existed before Bankruptcy.—Counter demands arising after bankruptcy cannot be offset. The mutual demands must have existed before the filing of the petition.⁸⁰ Thus, offset has been refused where a bank attempted to offset a check deposited the same day but shortly after the bankruptcy petition was filed.⁸¹

§ 1173. Offset Need Not Be Due, if Owning.—The debt sought to be set off need not be due at the date of adjudication, if owing.⁸²

Obiter, *Steinhardt v. National Bank*, 19 A. B. R. 72, 120 N. Y. App. Div. 255: " * * * it is well settled that this provision of the Bankruptcy Act relating to set-offs applies to any debt provable in bankruptcy, even though not then due."

80. Compare ante, § 1118½. In re *Michaelis & Lindeman*, 27 A. B. R. 299, 196 Fed. 718 (D. C. N. Y.).

Instances held not proper set-offs, because not existing before bankruptcy: Right of contribution in favor of bankrupt's cosurety where the obligation is taken up by the cosurety after the filing of the petition has been held not capable of being used as an offset against a claim of the estate against the comaker or cosurety existing at the time of the filing of the petition. In re *Bingham*, 2 A. B. R. 223, 94 Fed. 796 (D. C. Vt.).

Quere, In re *Dillon*, 4 A. B. R. 63, 100 Fed. 627 (D. C. Mass.), but this is doubtful law since such comaker's or cosurety's right of contribution for obligations paid after the bankruptcy is held to be a provable debt.

But the set-off contemplated by the Bankruptcy Act arising in case of mutual debts or mutual credits between the estate of the bankrupt and a creditor includes a liability that has accrued to a trustee which had not accrued to the bankrupt, when the claim and liability are mutual. In re *Crystal Springs Bottling Co.*, 4 A. B. R. 55, 100 Fed. 265 (D. C. Vt.).

No set-off of the testator's claim against his own bankrupt legatee where the testator's death occurs after the legatee's bankruptcy, nor although the will provides for set-off of debts against legacies. In re *Woods*, 13 A. B. R. 240, 132 Fed. 82 (D. C. Penn.).

Damages on attachment bond for wrongful attachment, accruing after the filing of the bankruptcy petition, may not be offset. In re *Bevins*, 21 A. B. R. 344, 165 Fed. 434 (C. C. A. N. Y.).

81. *Moore v. Third Nat'l Bank of Phila.*, 24 A. B. R. 568 (Pa. Super. Ct.).

82. In re *Ph. Semmer Glass Co.*, L't'd, 14 A. B. R. 25, 135 Fed. 77 (C. C. A. N. Y., affirming 11 A. B. R. 665), where the bankrupt's deposit in bank was permitted to be offset against his liability as endorser on paper not yet matured, but maturing within the year after the adjudication. *Seammion v. Kimball*, 92 U. S. 362; *N. Y. County Bk. v. Massey*, 11 A. B. R. 42, 192 U. S. 138 (The facts of this case are explained in *Carr v. Hamilton*, 129 U. S. 249, and in *Scott v. Armstrong*, 146 U. S. 499); *Frank v. Mercantile Nat'l Bk.*, 14 A. B. R. 125 (N. Y. Court Appeals); In re *Kalter*, 2 N. B. N. & R. 264; *Union Nat'l Bk. v. McKay*, 2 N. B. N. & R. 913; In re *Little*, 6 A. B. R. 681, 110 Fed. 621 (D. C. Iowa); *Myers v. Dickerson*, 5 A. B. R. 595 (D. C. N. Y.); *Ex parte Howard Nat'l Bk.*, Fed. Cases No. 6,764; In re *City Bk. of Sav.*, Fed. Cases No. 2,742.

But in the event the debt is not due, no affirmative judgment may be rendered thereon in favor of the defendant. *Frank as Tr. v. Mercantile Nat'l Bk.*, 14 A. B. R. 125 (N. Y. Court App.).

But see, *Irish v. Citizens Trust Co.*, 21 A. B. R. 39, 163 Fed. 880 (D. C. N. Y.), where precisely the opposite was held, the court refusing to allow the bankrupt to offset against a bankrupt's deposit his unmatured note. *Obiter*, *Taylor v. Nichols*, 23 A. B. R. 306, 134 App. Div. (N. Y.), 783, where a bankrupt's father who owed a debt to his daughter surrendered to her a note he held of his in excess of her debt to him.

Thus, unmatured notes may be offset. *Germania Saving & Trust Co. v. Loeb*, 26 A. B. R. 238, 188 Fed. 285 (C. C. A. Tenn.).

§ 1174. And May Be Only Contingently Owing.—Indeed a debt not due and only contingently owing may be set-off: as the bankrupt's liability as endorser on discounted paper not yet due may have offset against it a deposit in bank.⁸³

§ 1175. Separate Debt Not to Be Offset against Joint Debt.—A separate debt cannot be set off against a joint debt in bankruptcy unless growing out of a transaction or under circumstances establishing that the joint credit had been given on account of the separate debt.⁸⁴

§ 1176. Mutual Debts to Be between Same Parties, in Same Capacity.—But the mutual debts must be between the same persons, in the same capacity: thus, a debt due from a bankrupt to an individual partner of a solvent firm, may not be offset against a debt due the estate from the partnership;⁸⁵ although if the firm were insolvent a different rule might prevail.⁸⁶ Nor may an individual claim be set off against a trustee's claim.⁸⁷

Western Tie & Timber Co. v. Brown, 13 A. B. R. 451, 196 U. S. 502: "Now, as we have seen, from the facts found, it must be that the agreement between Harrison and the tie company obligated the latter, when it made the deduction from pay rolls, to remit to Harrison the amount of such deduction, irrespective of the account between itself and Harrison. It follows that as to such deductions the tie company stood towards Harrison in the relation of a trustee, and therefore, the case was not one of mutual credits and debts, within the meaning of the set off clause of the bankrupt law."

Nor can a debt due from a partner individually be set off against a judgment recovered by the firm's trustee for a partnership debt.⁸⁸

And it has been held, though by a divided court, that where the receiver and trustee in bankruptcy perform services and furnish material in endeavoring to complete the bankrupt's contract, the other party may not offset damages for the bankrupt's failure to complete the contract, at any rate not as against the receivers' and trustees' claim for materials and services though he might as against the portion of the bankrupt's work still unpaid for.

Howard v. Magazine & Book Co., 27 A. B. R. 296, 131 N. Y. Supp. (App. Div.) 916: "Receivers and trustees in bankruptcy are not obliged to continue to perform the contracts of the bankrupt, and damages growing out of such failures are properly claims against the bankrupt and not against the receivers or trustees as such. * * * But it is not apparent how a claim against a bankrupt

^{83.} *In re Ph. Semmer Glass Co. Lim.*, 11 A. B. R. 665 (Ref. N. Y.); *obiter*, *Morgan v. Wordell*, 6 A. B. R. 170 (Sup. Jud. Ct. Mass.).

^{84.} *In re Crystal Springs Bottling Co.*, 4 A. B. R. 55, 100 Fed. 265 (D. C. Vt.); *Gray v. Rollo*, 18 Wall. 629, 21 L. Ed. 927.

^{85.} *In re Shults*, 13 A. B. R. 84 (D. C. N. Y.).

^{86.} *Obiter*, *In re Shults*, 13 A. B. R. 84, 132 Fed. 573 (D. C. N. Y.); *In re Crystal Springs Bottling Co.*, 4 A. B. R. 55, 100 Fed. 265 (D. C. Vt.).

^{87.} *Howard v. Magazine & Book Co.*, 27 A. B. R. 296, 131 N. Y. Supp. 916.

^{88.} *In re T. M. Leshner & Son*, 25 A. B. R. 218, 176 Fed. 650 (D. C. Pa.).

may be set up as against a claim for services or material supplied by the trustee, even if they in doing so are but continuing a contract partly performed by the bankrupt."

§ 1177. Offset Must Be Provable Debt.—A set-off or counterclaim is not allowable in favor of any debtor of the bankrupt which is not itself provable against the estate; the claim sought to be set off must itself be a "provable debt."⁸⁹ Thus, a surety paying part of his principal's debt after adjudication of the principal, may offset the amount paid, by way of pro tanto subrogation to the creditor's claim, against a debt due from the surety to the estate.⁹⁰ But "provable" means provable in nature, not that it may be proved; thus, claims not filed within the year are nevertheless provable, though too late to be "proved."⁹¹

Similarly, the bankrupt has been allowed to offset a claim for unliquidated damages arising from the false representations of the creditor in inducing the bankrupt to enter into the contract of sale involved in the claim.⁹²

§ 1178. But Claim Not Proved within Year, Nevertheless Available as Offset.—But claims that are provable in their nature and have not been "proved" [filed] within the year are nevertheless available as offsets, if otherwise proper offsets.⁹³

Steinhardt v. National Park Bank, 19 A. B. R. 72, 120 App. Div. N. Y. 255: "Owing to the expiration of the year, the defendant had doubtless lost its right to prove its claim in bankruptcy; but that is of no consequence in the determination of this appeal, for it was entitled to the benefit of the set-off provision of the

⁸⁹ Bankr. Act, § 68 (b) (1). In re Ph. Semmer Glass Co. L't'd, 11 A. B. R. 665 (Ref. N. Y.), affirmed in 14 A. B. R. 25, 135 Fed. 77 (C. C. A. N. Y.).

In re Bingham, 2 A. B. R. 223, 94 Fed. 796 (D. C. Vt.), wherein it was held, a comaker of the bankrupt could not offset his right to contribution arising by his taking up the obligation since the bankruptcy against a claim existing against the comaker at the time of the filing of the petition. Such comaker's only right was to present the creditor's claim and take the dividends thereon. Compare, *quære*, In re Dillon, 4 A. B. R. 63, 100 Fed. 627 (D. C. Mass.).

Morgan v. Wordell, 6 A. B. R. 167, 178 Mass. 350, 59 N. E. 1037. In this case it was held, that a claim on which a preference had been received was on that account not a "provable" debt and yet might be used as an offset, if a "mutual credit." The right to offset the claim itself on which a preference had been received was denied on the ground that it was not "provable" against the estate, but the claim in the

form of a claim for indemnity was finally permitted to be offset, as being a mutual credit, the payment by the surety giving rise evidently to a claim in his own right for indemnity or contribution as to which he would not need to stand in the creditor's shoes.

In re Becher Bros., 15 A. B. R. 228, 139 Fed. 366 (D. C. Penn.): In this case the trustee in bankruptcy of a tenant was denied the right to offset against the landlord's claim for unpaid rent damages in tort for negligently permitting water to flow into tenant's premises.

⁹⁰ In re Dillon, 4 A. B. R. 63, 100 Fed. 627 (D. C. Mass.).

⁹¹ *Norfolk & W. Ry. Co. v. Graham*, 16 A. B. R. 615, 145 Fed. 610 (C. C. A. W. Va.); *Morgan v. Wordell*, 6 A. B. R. 167, 178 Mass. 350.

⁹² In re Harper, 23 A. B. R. 918, 175 Fed. 412 (D. C. N. Y.).

⁹³ In re Havens, 25 A. B. R. 116, 182 Fed. 367 (D. C. N. Y.); *Morgan v. Wordell*, 6 A. B. R. 167, 178 Mass. 350. See ante, § 733.

Bankruptcy Act regardless of the fact that it failed to prove its claim in bankruptcy."

Norfolk & W. Ry. Co. v. Graham, 16 A. B. R. 615, 145 Fed. 610 (C. C. A. W. Va.): "But we think it cannot be true that such failure to prove the claim to the excess in the bankruptcy proceeding leaves the company in the position of a mere debtor. Statutes of limitation are strictly construed. But even if the rule of construction were otherwise, the language of the clause in question and its context seem to us to plainly limit its effect to proceedings in bankruptcy. In enacting the Bankrupt Act, Congress could have had no reason for requiring a debtor creditor, whose claim against exceeds his debt to the bankrupt, to prove the excess and insist upon his rights as a creditor of the estate. And hence there was no reason for penalizing such failure by imposing a limitation upon the right of a person thus situated who does not wish to prove and claim the excess. The full purpose of § 57n seems to us to be subserved when it is held that the limitation applies merely to claims sought to be asserted in the bankruptcy proceeding.

"We think the true solution of the question before us is that the counterclaim which may be set off in an independent action brought by the trustee is (subject to the restrictions of § 68b, 30 Stat. 565 [U. S. Comp. St. 1901, p. 3,450]) one that is provable in its nature, and need not necessarily be one that has been, or may yet be, proved in the bankruptcy proceeding."

This rule would seem to apply to cases where the trustee in bankruptcy has recovered a preference and the preferential transferee has failed to prove his claim in the bankruptcy court within the year.

Yet, compare, *obiter*, *Ommen, Trustee, v. Talcott*, 23 A. B. R. 570, 175 Fed. 259, 261 (D. C. N. Y.): "In equity his claim as beneficiary must be subject to the same rules of limitation as though he applied in the bankruptcy court for his beneficial interest pro rata in the funds of that court. In other words, it is a case in which a court of equity ought to observe the same limitation in giving a remedy on the cross-bill as the claim itself would be subject to were suit brought upon it in the tribunal which normally has jurisdiction over it. Besides, I think that Mr. Czaki has shown that the cases which seem to permit a claim of this character to be set off are all cases arising in bankruptcy, and that a court of equity has never attempted to allow a claim at a time when it could no longer be proved. All these were cases originally in bankruptcy, and, if so, they are equally authorities to the defendant in a bankruptcy court as they are in a court of equity. It is true that *Page v. Rogers*, 211 U. S. 575, 21 Am. B. R. 496, 53 L. Ed. 332, was a case in which the decree was in equity, but in that case the court did not allow the set-off in the suit itself, but, on the contrary, directed the defendant to file his proof of claim in the bankruptcy court. On the other hand, there is a hope of the substantial determination of this litigation, if the cross-bill is not interjected at the present time, and, in view of the extraordinary delays which the suit has already suffered, I am not in the least disposed to give the parties any further grounds for procrastination. I will not, however, deprive the defendant of the use of so much of the recovery as he is apparently entitled to under his claim in bankruptcy, and therefore I will let him retain in his hands that proportion of his assets which his claim in bankruptcy, if filed, represents of the total of all claims filed, including his own. This he may do if at the time the decree is entered he has already filed his proof of claim in the bankruptcy court. Of course, a certain portion of his dividend so retained he will have

to pay over as his proportion of the expenses of administration, but that cannot be ascertained at the present time. When I come to decide the case and direct the final decree, I will therefore allow the defendant to retain his proportion of his claim in bankruptcy out of the proceeds of this suit. If the complainant desires, the defendant will be obliged to give security for the payment of the portion so retained, provided he does not succeed in proving his claim in bankruptcy for any part or all of the same, and the complainant will be permitted at any time to apply at the foot of the decree for a modification as to that portion, if the defendant procrastinate in pressing his claim in bankruptcy, or to compel him to pay his share of the expenses."

§ 1179. Voidable Preference Not Available as Offset in Favor of Preferred Creditor.—Preferences voidable under § 60 (a) and (b) are not allowable as set-offs to claims against preferred creditors on the ground that the preferences and the claims constitute mutual debts and credits.⁹⁴

Inasmuch as a debt upon which a preference has been given is nevertheless "provable" though not "allowable" (as noted, ante, § 632), the refusal to permit the offsetting of preferences must either be based on general principles of statutory construction or upon the interpretation of the term "provable" here to mean "allowable."

§ 1179½. But Dividend Available as Offset in Favor of Preferred Creditor.—But the dividend to which the preferred creditor would be entitled upon recovery of the preference by the trustee, may be offset by the preferred creditor.⁹⁵

94. *Western Tie & Timber Co. v. Brown*, 12 A. B. R. 111 (C. C. A. Ark.), reversed in 13 A. B. R. 447, 196 U. S. 502.

Obiter, *Mason v. Herkimer Co. Bank*, 22 A. B. R. 733, 172 Fed. 529 (C. C. A. N. Y.); compare, *In re White* (*Froehling v. Amer. Trust & Savings Bank*), 24 A. B. R. 197, 177 Fed. 194 (C. C. A. Ill.), although the decision in this case is better placed upon the doctrine of § 1184, post.

In re Ryan, 5 A. B. R. 396, 105 Fed. 760 (D. C. Ills.): Although this was a case of so-called "innocent preferences" before the Amendment of 1903, yet the principle involved is the same. "Cash payments on account (if received with reasonable grounds of belief, etc.,) made within four months before the filing of the bankruptcy petition, are not included in the mutual debts and credits contemplated by § 68."

Compare, as to deposit in bank being available as offset, *New York Co. Nat. Bk. v. Massey*, 11 A. B. R. 42, 192 U. S. 138 (reversing *In re Stege*, 8 A. B. R. 515, 116 Fed. 342 (C. C. A. N. Y.)); *Trust & Sav. Bk. v. Trust Co.*, 224 U. S. 152, 30 A. B. R. 624; also, compare

to same effect, *In re Elsasser*, 7 A. B. R. 215 (Ref. Penn.). Also, compare, inferentially, *Morgan v. Wordell*, 6 A. B. R. 167, 59 N. E. 1037 (Mass. Sup. Jud. Ct.); also, compare, *obiter*, *In re Dillon*, 4 A. B. R. 63, 100 Fed. 627 (D. C. Mass.); also, compare, *In re Scherzer*, 12 A. B. R. 451, 130 Fed. 631 (D. C. Iowa).

Preferential Transferee's Reimbursement for Care of Property Meanwhile.—It has been held that the preferential transferee will not be allowed, by way of set-off, a claim for money advanced or expended in connection with the property while it was in his possession; but that such claim must be properly presented against the estate in bankruptcy. *Bank of Wayne v. Gold*, 26 A. B. R. 722 (App. Div. N. Y.). But compare ante, § 775, note, and post, § 1734½.

95. See ante, §§ 716, 717, 717½, 733, 775, 1178. Compare, post, § 1185, as to dividend on stockholding creditor's claim being offset against unpaid stock subscriptions. *Ommen, Trustee v. Talcott*, 23 A. B. R. 570, 175 Fed. 259, 261 (D. C. N. Y.), quoted at § 1178.

And, where a preferential transferee had failed to set up his claim to dividend by way of cross-bill, the court protected him by an order permitting him to retain sufficient of the funds, on the giving of a bond, to cover his possible dividend.⁹⁶

§ 1180. But General Deposits in Bank Available to Bank as Set-Off, if Not Applied by Bankrupt on Bank's Claim.—A deposit in bank is not a preference, even when applied upon a debt with full knowledge of the debtor's insolvency, where it has been made as a general deposit, subject to check and creating the relation of debtor and creditor, and not made as a deposit to pay a particular debt; and, therefore, not being a preference, it is available as an offset to the debtor's note or other debt.⁹⁷

New York County Nat. Bk. *v.* Massey, 11 A. B. R. 42, 192 U. S. 138, reversing *In re Stege*, 8 A. B. R. 515 (C. C. A. N. Y.), where the United States Supreme Court held, that a deposit of money within four months of bankruptcy, with a bank upon an open account subject to check, may be set off, the Supreme Court saying: "A deposit of money to one's credit in a bank does not operate to diminish the estate of the depositor, for when he parts with the money he

96. *Ommen, Trustee v. Talcott*, 23 A. B. R. 570, 175 Fed. 259, 261 (D. C. N. Y.).

97. Compare post, "Fifth Element of Preference—Transfer," § 1341, et seq.; also see *Trust & Sav. Bk. v. Trust Co.*, 224 U. S. 152, 30 A. B. R. 624; *Studley v. Boyleston Nat. Bk.*, 229 U. S. 523, 30 A. B. R. 161 (aff'g S. C.), 29 A. B. R. 169, 200 Fed. 249; *Studley v. Boyleston Bk.*, 29 A. B. R. 169, 200 Fed. 249 (C. C. A. Mass.), quoted at § 1329 and § 1341; *In re Elsasser*, 7 A. B. R. 215 (Ref. Penn.); *In re Myers & Charni*, 3 A. B. R. 760 (D. C. Ind.); *In re Hill Co.*, 12 A. B. R. 221, 120 Fed. 315 (C. C. A. Ills.); *In re Little*, 6 A. B. R. 681, 110 Fed. 621 (D. C. Iowa); *In re Scherzer*, 12 A. B. R. 451, 130 Fed. 631 (D. C. Iowa); *In re Shults*, 13 A. B. R. 84 (D. C. N. Y.); *West v. Bk. of Lahoma*, 16 A. B. R. 733 (Sup. Ct. Okla.); *In re Medarsi-Vine Carriage Co.*, 17 A. B. R. 897 (Ref. Ohio); *Whitaker v. Crowder State Bank*, 25 A. B. R. 876 (Sup. Ct. Okla.); *In re Percy Ford Co.*, 28 A. B. R. 919, 199 Fed. 334 (D. C. Mass.); *Germania Savings & Trust Co. v. Loeb*, 26 A. B. R. 238, 188 Fed. 285 (C. C. A. Tenn.); *Steinhardt v. National Bank*, 19 A. B. R. 72, 120 App. Div. (N. Y.) 255. Compare post, §§ 1297, 1341; *Booth v. Prete*, 22 A. B. R. 579, 81 Conn. 636, 71 Atl. 938; obiter, *Irish v. Citizens Trust Co.*, 21 A. B. R. 39 (D. C. N. Y.).

And it makes no difference that the notes were not yet due. *Germania*

Savings & Trust Co. v. Loeb, 26 A. B. R. 238, 188 Fed. 285 (C. C. A. Tenn.).

Rule conceded but held not applicable to offset of deposit of a check on same day though before precise hour of filing bankruptcy petition. *Moore v. Third Nat'l Bk. of Phila.*, 24 A. B. R. 568 (Pa. Superior Ct.).

In re Meyer & Dickinson, 5 A. B. R. 593, 106 Fed. 828 (D. C. N. Y.): Bank issuing due bill on depositor's account in ignorance of depositor's general assignment, may, on bankruptcy of depositor later occurring, recover the due bill from the trustee for purposes of offset against unmatured notes of depositor. To same effect (1867), *In re Petrie*, 7 N. B. Reg. Fed. Cases 11,040; to same effect (1867), *Blair v. Allen*, 3 Dill. 101, Fed. Cas. 1,483; to same effect (1867), *Scammon v. Kimball*, 92 U. S. 362; compare, also, to same effect (1867), *Traders' Bk. v. Campbell*, 14 Wall. 87; contra, *In re Keller*, 6 A. B. R. 621, 109 Fed. 118 (D. C. Iowa).

And the right of offset exists where the bankrupt's liability was contingent, as endorser. *In re Ph. Semmer Glass Co., Lim.*, 11 A. B. R. 665 (Ref. N. Y.), affirmed in 14 A. B. R. 25, 135 Fed. 77 (C. C. A.); obiter, *Morgan v. Wordell*, 6 A. B. R. 170 (Mass. Sup. Jud. Court); also, see ante, § 1174.

It has been held that the bank's right of offset may not be exercised as to notes not yet due. *Irish v. Citizens Trust Co.*, 21 A. B. R. 39 (D. C. N. Y.).

creates at the same time, on the part of the bank, an obligation to pay the amount of the deposit as soon as the depositor may see fit to draw a check against it. It is not a transfer of property as a payment, pledge, mortgage, gift or security. It is true that it creates a debt, which, if the creditor may set it off under § 68, amounts to permitting a creditor of that class to obtain more from the bankrupt's estate than creditors who are not in the same situation, and do not hold any debts of the bankrupt subject to set-off. But this does not, in our opinion, operate to enlarge the scope of the statute defining preferences so as to prevent set-off in cases coming within the terms of § 68a. If this argument were to prevail it would, in cases of insolvency, defeat the right of set-off recognized and enforced in the law, as every creditor of the bankrupt holding a claim against the estate subject to reduction to the full amount of a debt due the bankrupt receives a preference in the fact that to the extent of the set-off he is paid in full."

But doubtless if the deposit is not all the time subject to check, but is a deposit against the particular debt, it would amount to a method of paying the debt by "transfer" and would be a preference, if other conditions of a preference also existed. However, the giving to the bank of a check on the deposit to pay the note has been held to be merely the recognition and voluntary exercise of the right of offset already existing and not to be a preference.^{97a}

And the rule is not changed where a bank holds ample security for the debt at the time of bankruptcy, but, by delay, the security depreciates and leaves a deficit: the deposit may still be offset.⁹⁸ And the date of the filing of the bankruptcy petition is the date at which the provability is to be tested.⁹⁹ Similarly, it would appear that the date of the filing of the bankruptcy petition is the date for determining the status of the deposit;¹ and it has been held that fractions of a day may be disregarded, where substantial justice is thus done;² so that in one case the deposit of a check on the identical day of the filing of the bankruptcy petition, though actually before the filing thereof (especially since it was deposited for collection

^{97a}. *Studley v. Boyleston Nat. Bk.*, 229 U. S. 523, 30 A. B. R. 161, affirming S. C., 29 A. B. R. 649, 200 Fed. 249 (C. C. A. Mass.).

⁹⁸. *Steinhardt v. National Bank*, 19 A. B. R. 72, 120 App. Div. (N. Y.) 255 reversing 18 A. B. R. 86, 52 Misc. (N. Y.) 464.

Bank may be allowed to amend its claim by deducting deposits by way of offset. *In re Myers & Charni*, 3 A. B. R. 760 (D. C. Ind.).

Offset against claim upon an endorsement by bankrupt before maturity of paper. *In re Ph. Semmer Glass Co. L't'd*, 11 A. B. R. 665 (Ref. N. Y.), affirmed in 14 A. B. R. 25, 135 Fed. 77 (C. C. A. N. Y.); *obiter*, *Morgan v. Wordell*, 6 A. B. R. 170 (Mass. Sup. Jud. Ct.).

No offset by retaining to apply on

own claim against bankrupt store-keeper funds deducted from employees' wages to pay storekeeper for supplies furnished the employees; one relation is a trust relation, the other individual. *Western Tie & Timber Co. v. Brown*, 13 A. B. R. 447, 196 U. S. 502, reversing 12 A. B. R. 111.

⁹⁹. *Steinhardt v. Nat'l Bk.*, 18 A. B. R. 87, 52 Misc. (N. Y.) 465, reversed, on other grounds, in 19 A. B. R. 72, 120 App. Div. N. Y. 255.

¹. (Assumed as rule) *Moore v. Third Nat'l Bk. of Phila.*, 24 A. B. R. 568 (Pa. Superior Court).

². Impliedly, *Moore v. Third Nat'l Bk. of Phila.*, 24 A. B. R. 568 (Pa. Superior Court): *In re Michaelis & Lindeman*, 27 A. B. R. 299, 196 Fed. 718 (D. C. N. Y.).

merely and not collected until afterwards) was held as occurring at the same instant with the filing of the bankruptcy petition and hence not available as an offset.³

§ 1181. Creditor Selling Claim to Effect Indirect Preference by Purchaser's Using Claim as Offset to Purchase Price.—A creditor of the bankrupt cannot avoid the prohibitions of the Act against preferences by assigning his claim to one who in turn uses it as part of the purchase price of assets bought from the bankrupt.⁴

Similarly, a creditor who purchased a portion of the bankrupt's property, whilst the bankrupt's business was in the hands of a creditors' committee (of which the purchasing creditor was a member), has been refused the right of offsetting his claim against the unpaid purchase price.⁵

§ 1182. Offsets Purchased with Knowledge of Insolvency or to Use as Offset, etc., Not Allowable.—But a set-off or counterclaim is not allowable in favor of any debtor of the bankrupt which was purchased by or transferred to him after the filing of the petition, or within four months before such filing, with a view to such use and with knowledge or notice that such bankrupt was insolvent, or had committed an act of bankruptcy.⁶

Western Tie & Timber Co. v. Brown, 13 A. B. R. 452, 196 U. S. 502: "To allow the set-off under the circumstances disclosed would violate the plain intendment of the inhibition contained in clause b (2) of § 68. * * * That is to say, whether or not the trust relation was engendered, the result would still be that the tie company, within the prohibited period, and with knowledge of the insolvency of Harrison, acquired the claims of the latter against the laborers, with a view to using the same by way of payment or set-off, so as to obtain an advantage over the other creditors which it was not lawfully entitled to do."

[Not so purchased] *Trust & Savings Bank Co. v. Trust Co.*, 224 U. S. 152; 30 A. B. R. 624: "It is the main purpose of this statute, as its terms show, to prevent debtors of the bankrupt from acquiring claims against the bankrupt for use by way of set-off and reduction of their indebtedness to the estate. There is no question of the solvency of Prince when he deposited the money to secure the certificates, and what was done was not the acquisition of a claim against Prince with a view to setting it off against the bank's indebtedness on the certificates, but was the satisfaction, without diminution of the estate of the

3. *Moore v. Third Nat'l Bk. of Phila.*, 24 A. B. R. 568 (Pa. Superior Ct.). In re *Michaelis v. Lindeman*, 27 A. B. R. 299, 196 Fed. 718 (D. C. N. Y.).

4. *Hackney v. Hargreaves Bros.* (Raymond Bros. Clark Co.), 13 A. B. R. 164, 68 Neb. 634 (Sup. Ct. Neb.).

5. In re *White* (*Froehling v. Amer. Trust & Savings Bank*), 24 A. B. R. 197, 177 Fed. 194 (C. C. A. Ill.).

6. Bankr. Act, § 68 (b) (2). In re *Shults*, 14 A. B. R. 378 (D. C. N. Y., affirming 13 A. B. R. 84), which was a

case of assigning claims for the purpose of obtaining offset after bankruptcy, or at any rate, with knowledge of the impending bankruptcy. *Obiter*, *Stich v. Berman*, 15 A. B. R. 467 (N. Y. Sup. Ct. App. Div.).

National Bank of Newport v. National Herkimer Co. Bank, 28 A. B. R. 218, 225 U. S. 178. Compare, in re *White*, 24 A. B. R. 197, 177 Fed. 194 (C. C. A. Ill.). Compare, analogously, ante, § 1179½.

bankrupt, of possible claims of others, who, in the event of Prince's default, would have been entitled to the deposits represented by the certificates. We do not think such transaction comes within the language or reason of § 68b."

Compare, *Hackney v. Hargreaves Bros.*, 13 A. B. R. 164 (Neb. Sup. Ct.): "A creditor of a bankrupt cannot escape the consequences of the Bankrupt Act regarding unlawful preferences by assigning his account to a purchaser of the property of the bankrupt, under an arrangement whereby such purchaser offers to assume the liability and satisfy such account, contingent upon the purchase of the bankrupt's property and where in the sale of such bankrupt's property as a part of the consideration, such purchaser agrees to and assumes such liability, and reserves from the purchase price an amount sufficient to satisfy the same.

"In such a case the legal effect of the transaction is to appropriate out of the assets of the bankrupt the amount required and used in the satisfaction of such claim by the purchaser assuming the liability, and other essential elements not being lacking, an unlawful preference in favor of such creditor results therefrom."

But the provision is only applicable where the trustee is one of the parties. It is not applicable as between strangers upon claims assigned and claims owing by the bankrupt.⁷

§ 1183. Burden of Proof of Propriety of Offset on Debtor.—The burden of proof is on the debtor seeking to use the offset to show it was received before the bankruptcy and without knowledge of the impending bankruptcy.⁸

§ 1184. Supervening Insolvency Destroying Right of Offset.—Wherever supervening insolvency would destroy the right of set-off, had there been no proceedings in bankruptcy, it will likewise destroy it in bankruptcy. Thus, a creditor who has purchased a portion of the bankrupt's property whilst it was in charge of an advisory creditors' committee, may not offset his claim against the unpaid purchase price;⁹ although, no doubt, the creditor could, by proper proceedings, offset the dividend to which he might be entitled against the unpaid purchase price.

§ 1185. Thus, Stockholding Creditor May Not Offset against Unpaid Subscriptions.—Thus a stockholder who is also a creditor may not offset his claim against his liability for unpaid stock subscription, after the corporation becomes insolvent.¹⁰

Kiskadden v. Steinle, 29 A. B. R. 346, 203 Fed. 374 (C. C. A. Ohio): "However, we think the true interpretation of § 68a and b and of such rule is, that after the corporation becomes insolvent, any sum due upon a stock subscription is impressed with the character of a trust in favor of all the creditors alike, except only such as may have given credit to the company with knowledge of

7. *Stich v. Berman*, 15 A. B. R. 467 (N. Y. Sup. Ct. App. Div.).

8. *In re Shults*, 14 A. B. R. 378, 135 Fed. 623 (D. C. N. Y.).

9. *In re White* (*Froehling v. Amer. Trust & Savings Bank*), 24 A. B. R.

197, 177 Fed. 194 (C. C. A. Ill.), although not placed upon this ground.

10. *In re Howe Mfg. Co.*, 27 A. B. R. 477, 193 Fed. 524 (D. C. Ky.); *In re Standard Dairy & Ice Co.*, 20 A. B. R. 321 (Ref. D. C.). Compare, similar propositions, ante, §§ 805½, 810¾.

the scheme of stock issue. Hence, to apply such an unpaid subscription as a set-off to an ordinary claim held by the subscriber against the corporation would be to appropriate the rights of the other creditors in the subscription debt to the exclusive benefit of the person owing it; or, on the other hand, it might, as respects his co-stockholders, subject him to the payment of more than his ratable share of the bankrupt's debts. It cannot be said, then, that the debts in question are in their nature both mutual and in the same right; nor that after the bankruptcy there was any reason for enforcing stockholder's liability or Bauman's ratable share thereof except for the equal benefit of all the creditors."

In *re Albert Goodman Shoe Co.*, 3 A. B. R. 200, 96 Fed. 949 (D. C. Penna.): "He cannot be permitted to diminish a fund that he is under obligation to increase and thereby deprive the other creditors of money that it would be his duty immediately to return. If the Company had continued to be solvent, it might or might not have been at liberty, under all circumstances, to set-off his subscription against his liability on the note. That point is not now involved for the fact of insolvency has supervened, and this creates a situation in which the rights of other creditors must also be considered. It would be highly inequitable to allow him to apply a part of the assets for his own benefit, until he has put into the funds money that he justly owes. He must cease to be a debtor before he can enforce his claim as a creditor."

Babbitt v. Read, 23 A. B. R. 254, 173 Fed. 712 (U. S. C. C. N. Y.): "Coming to the second defense, the set-off alleged is not available against the trustee in bankruptcy, because it involves no mutual debt or credit between the stockholder and the estate of the bankrupt, within § 68 of the Bankruptcy Act. *Sawyer v. Hoag*, 17 Wall. 610, 21 L. Ed. 731. When the Central Trust Company, as trustee under the mortgage, distributes among the bondholders it represents the dividend paid it by the trustee in bankruptcy, so far as the same has been collected from the stockholders, this equity can be adjusted. In that proceeding the paying stockholders will get back whatever they are entitled to as bondholders. The trustee in bankruptcy is not concerned in settling the equities of the bondholders and the stockholders inter sese. If, however, for the protection of creditors other than the bondholders, it should prove necessary to settle these equities in the bankruptcy court, that court has power to do so, because it is necessary for the proper distribution of the bankrupt's estate."

A dividend declared by the bankrupt corporation when not earned, of course may not be offset by a stockholder against the trustee's suit for unpaid stock subscription.¹¹

Nor may a stockholder, after the bankruptcy of the corporation, rescind his stock subscription for fraud or misrepresentation and present his claim for moneys paid by him, for sharing in the bankruptcy dividends; and this is so, notwithstanding the fraud was not discovered before.¹²

Perhaps such instances should rather come under the subject of the creditor's title taken by the trustee.

However, the dividend on the stockholding creditor's claim may, without doubt, be offset against his unpaid subscription.¹³

11. *Roney v. Crawford*, 24 A. B. R. 160 Fed. 573 (C. C. A. Mo.), quoted at 638 (Ga.). § 805½.

12. *Scott v. Abbott*, 20 A. B. R. 335,

13. Compare analogous doctrine as

§ 1186. Supervening Insolvency Creating Right of Offset.—On the other hand wherever supervening insolvency would give rise to the right of set-off, the right is enforceable in bankruptcy.¹⁴

Schuler v. Israel, 120 U. S. 606: "While it may be true that in a suit brought by Israel against the bank it could, in an ordinary action at law, only make plea of set-off of so much of Israel's debt to the bank as was then due, it could by filing a bill in chancery in such a case, alleging Israel's insolvency, and that, if it was compelled to pay its own debt to Israel, the debt which Israel owed it, but which was not due would be lost, be relieved by a proper decree in equity."

And this right may be exercised by the trustee against an insolvent stockholder who is also a creditor.¹⁵

§ 1187. No Judgment against Trustee for Excess of Offset.—But such claims can only be used for set-off—no affirmative judgment for any excess can be rendered against the trustee;¹⁶ although of course the excess may be presented as a claim against the estate.¹⁷

§ 1188. Likewise, No Judgment in Bankruptcy Proceedings against Claimant Where Estate's Claim Exceeds Claimant's.—Likewise there may be no judgment in the bankruptcy proceeding against the claimant where the estate's offset exceeds the creditor's claim. The trustee must seek his remedy by plenary action.¹⁸

to offsetting bankruptcy dividends against preferences, ante, § 1179½. Compare, obiter, inferentially, *In re Alleman Hardware Co.*, 22 A. B. R. 871, 172 Fed. 611 (D. C. Pa.), quoted on other points ante, § 976; inferentially, *Babbitt v. Read*, 23 A. B. R. 254, 173 Fed. 712 (U. S. C. C. N. Y.), quoted at § 1185; (1867) obiter, *Wilbur v. Stockholders of the Corporation*, 18 Nat. Bankr. Reg. 179.

14. Compare, to same effect, *Carr v. Hamilton*, 129 U. S. 249. *In re Meyer & Dickinson*, 5 A. B. R. 593 (D. C. N. Y.): In this case a bank paid money by due bill in ignorance of a depositor's general assignment; the court held, that it might on the subsequent bankruptcy of the depositor, recover the due bill for the purpose of offset, even in Pennsylvania whose laws prohibit, under other circumstances, the offsetting of deposits against unmatured notes.

Special Deposit by Tenant with Landlord to Secure Covenants of Lease, on Landlord's Subsequent Bankruptcy to Be Applied According to Terms of Deposit and Not to Be Used as Offset to Rents Accruing after Bankruptcy.—Where a tenant deposited a fund with his landlord for the faith-

ful performance of the covenants of the lease during its entire term, same to be applied on the last six months' rent, the landlord's bankruptcy will not entitle the tenant to offset the deposit against rents accruing after bankruptcy and before completion of the term of the lease. *In re Banner*, 18 A. B. R. 62, 149 Fed. 636 (D. C. N. Y.).

15. Inferentially, *Babbitt v. Read*, 23 A. B. R. 254, 173 Fed. 712 (U. S. C. C. N. Y.), quoted at § 1185.

16. *Trustee v. Mercantile Nat'l Bk.*, 14 A. B. R. 125 (N. Y. Court App.).

17. *Matter of Havens*, 25 A. B. R. 116, 182 Fed. 367 (D. C. N. Y.); obiter, *In re T. M. Leshner*, 25 A. B. R. 218, 176 Fed. 650 (D. C. Pa.).

18. See post, general subject of "Jurisdiction over Adverse Claimants," ch. XXXIII; analogously, *Fitch v. Richardson*, 16 A. B. R. 835, 147 Fed. 196 (C. C. A. Mass.). Similarly, § 764.

Obiter, *In re T. M. Leshner*, 25 A. B. R. 218, 176 Fed. 650 (D. C. Pa.); analogously, *In re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.); apparently, contra, *In re White (Froehling v. Amer. Trust & Savings Bank)*, 24 A. B. R. 197, 177 Fed. 194 (C. C. A. Ill.).

SUBDIVISION "F."

APPLICATION OF PAYMENTS.

§ 1189. **Application of Payments.**—The rights of the parties as to the application of payments remain unimpaired by the debtor's subsequent bankruptcy, and the trustee takes title subject thereto.¹⁹

§ 1190. Thus, **Creditor's Right to Apply in Absence of Debtor's Instructions.**—The right of a creditor to apply payments as he may desire, in the absence of instructions from the debtor before the application, is unimpaired by the debtor's subsequent bankruptcy; although thereby the creditor is permitted to apply them on an unsecured debt rather than on a secured debt;²⁰ or on a claim not entitled to priority rather than on a priority claim.²¹

But if he apply payments received during the four months period before bankruptcy (limited for avoiding preferences) on wages earned before the statutory period of three months (limited for priority of wages), thus leaving a priority claim for the full amount earned within the statutory three months, he must surrender the preferential payments, for the payments were not made on claims entitled to priority,²² but not, if he did not receive the payments with reasonable grounds of belief, etc.²³ And a creditor may not apply a payment upon an unpaid check where the check was given before and the payment made after, a new invoice of goods was sold on credit to the insolvent, so as to enable him to offset the invoice against the payment as being a "new credit" subsequent to a preference.²⁴

§ 1191. **Application to Be as Equity Requires, in Absence of Directions.**—The duty of the court to apply payments as equity may require in the absence of direction from the debtor in the first instance and

19. Instance, application of payments, *Hoffschlaeger Co. v. Young Nap*, 12 A. B. R. 517 (D. C. Hawaii): Account with partnership continued with its successor, a corporation, payments applied by creditors to partnership claim.

Instance, *In re Porterfield*, 15 A. B. R. 11, 138 Fed. 192 (D. C. W. Va.): Agent and principal: Tax collector, short in his accounts, receipts his own tax bills, nevertheless held, his taxes paid and moneys in his hands turned over to his principal could not later be applied by the court first on other taxes then on his own.

Instances, *In re Johnson*, 11 A. B. R. 138 (D. C. N. Car.); *In re King Co.*, 7 A. B. R. 619, 113 Fed. 110 (D. C. Mass.); *In re Bailey*, 7 A. B. R. 26, 112 Fed. 406 (D. C. Vt.); *Zartman v. Hines*, 6 A. B. R. 139 (Ref. N. Y.); *In re Tanner*, 6 A. B. R. 196 (D. C. N. Y.).

20. *In re Johnson*, 11 A. B. R. 138 (D. C. N. Car.); *Hoffschlaeger v. Young Nap*, 12 A. B. R. 517 (D. C. Hawaii).

21. *In re Van Wert Machine Co.*, 26 A. B. R. 597, 186 Fed. 607 (D. C. Mass.); *In re Andrews*, 19 A. B. R. 441 (Ref. N. Car.). Also, see post, § 2179½. But compare, *In re Flick*, 5 A. B. R. 465, 105 Fed. 503. And in some States the court, in the absence of application by the parties, will apply payments most favorably to the debtor rather than to the creditor, *In re McIntyre Bros.*, 21 A. B. R. 588 (Ref. Miss.).

22. *In re King Co.*, 7 A. B. R. 619, 113 Fed. 110 (D. C. Mass.).

23. *In re Andrews*, 19 A. B. R. 441 (Ref. N. Car.).

24. *In re Bailey*, 7 A. B. R. 26, 112 Fed. 406 (D. C. Vt.).

of the creditor in the second instance, is unimpaired.²⁵ And application will be made by a court of equity, first upon the interest and then upon the principal; ²⁶ and first upon the prior indebtedness, even though thereby the creditor is enabled to claim right of offset for unsecured new credits,²⁷ or to claim priority for the later items.²⁸

Likewise, where, under one continuous arrangement, book accounts were assigned as collateral each time a lender made an advancement, the proceeds of each account, when collected, were applied first to the particular note for which the account was assigned, then any surplus to the debtor's general account.²⁹

SUBDIVISION "G."

SPECIFIC DEFENSES AND RIGHTS OF BANKRUPT TO WHICH TRUSTEE SUCCEEDS.

§ 1192. Trustee Succeeds to Bankrupt's Defenses and Rights.

—On the other hand, the trustee is entitled to urge all the rights and all the defenses the bankrupt might have urged had there been no bankruptcy.³⁰

Drew v. Myers, 22 A. B. R. 656, 81 Neb. 750: "We think it safe to say that the trustee of a bankrupt may maintain any action which the bankrupt might have maintained but for the intervention of the bankruptcy, and it is not necessary in such a case for him to state that the property already in his hands is insufficient to pay the debts of the bankrupt. It is only when he brings an action which is in the nature of a creditor's bill that he is required to make such an allegation."

Amendment of 1910.—The Amendment of 1910, giving the trustee also the title of a creditor levying process as to property in the custody of the bankruptcy court, and of a creditor with execution unsatisfied as to property not in such custody, does not prevent the trustee's succession to all the bankrupt's defenses and rights; the trustee still is entitled to urge all the rights and all the defenses the bankrupt might have urged had there been no bankruptcy.³¹

²⁵. *Zartman v. Hines*, 6 A. B. R. 139 (Ref. N. Y.); *In re Tanner*, 6 A. B. R. 196 (Ref. N. Y.).

²⁶. *Zartman v. Hines*, 6 A. B. R. 139 (Ref. N. Y.).

²⁷. *In re Tanner*, 6 A. B. R. 196 (Ref. N. Y.).

Likewise Application of Securities to Be Made in Accordance with Contract.—Where a fund has been deposited as security with one subsequently becoming bankrupt such fund is to be applied in accordance with the contract and the bankruptcy will not permit a change of such application. Impliedly,

In re Banner, 18 A. B. R. 61, 149 Fed. 936 (D. C. N. Y.).

Creditor having two securities, whether trustee can oblige him to exhaust the other security before resorting to security on which trustee also has lien. *In re Currie (Austin)*, 26 A. B. R. 345, 185 Fed. 263 (C. C. A. N. Y.).

²⁸. *In re Van Wert Mach. Co.*, 26 A. B. R. 597, 186 Fed. 607 (D. C. Mass.).

²⁹. *Young v. Upson*, 8 A. B. R. 377, 115 Fed. 192 (U. S. C. C. N. Y.).

³⁰. *In re Martin*, 27 A. B. R. 151 (Ref. Tex.).

³¹. Bankr. Act, § 70a.

§ 1193. May Interpose Bar of Statute of Limitations.—The trustee may plead the statute of limitations and indeed it is his duty to do so.³²

In *re Wooten*, 9 A. B. R. 247, 250, 118 Fed. 670 (D. C. N. Car.): "It is the duty of the trustee to plead the statute of limitations, especially when required by creditors whom he represents."

Impliedly, In *re Lorillard*, 5 A. B. R. 603, 604, 107 Fed. 677 (C. C. A. N. Y.): "Two objections are urged to the allowance of these claims, (a) that they were outlawed at the time the petition was filed. * * * What written statement will be sufficient to take a case out of the operation of the statute of limitations is regulated by the provisions of the New York Code of Civil Procedure. Discussions of the general subject found in the opinions of the Federal courts and of courts of other States are, therefore, unpersuasive. The statute of New York, as interpreted by the New York courts, is controlling."

The fact that the bankrupt, after the filing of the petition, executes an acknowledgment of indebtedness wherein the statute of limitations is waived, does not prevent the trustee from setting up the statute as a bar to such indebtedness.³³

It is also held, that any creditor may interpose the defense;³⁴ but this rule would properly apply only where no trustee had yet been appointed, or where the creditor's special rights, as distinguished from the rights of all the other creditors, are involved.

§ 1194. May Urge Statute of Frauds.—So, also, he may plead or interpose the Statute of Frauds.³⁵

§ 1194½. May Plead Estoppel.—So also, he may plead estoppel.³⁶

§ 1195. May Plead Illegality or Ultra Vires.—So, also, the trustee may plead and urge illegality,³⁷ and ultra vires.³⁸

§ 1196. May Plead Usury.—So, also, he may plead usury although this defense is usually said to be one purely personal to the debtor.³⁹

^{32.} In *re Farmer*, 9 A. B. R. 19, 116 Fed. 763 (D. C. N. Car.).

Thus, to wife's claim of vendor's lien for money advanced for husband, bankrupt, 25 years before, In *re Teter*, 23 A. B. R. 223, 173 Fed. 798 (D. C. W. Va.).

^{33.} In *re Zorn & Co.*, 27 A. B. R. 433, 193 Fed. 299 (D. C. Pa.).

^{34.} In *re Lafferty & Bros.*, 10 A. B. R. 290, 122 Fed. 558 (D. C. Penn.). See also, other instances, In *re Lorillard*, 5 A. B. R. 602, 107 Fed. 677 (C. C. A. N. Y.).

^{35.} Instance, *Zartman v. Hines*, 6 A. B. R. 139 (Ref. N. Y.).

^{36.} Instance, In *re Cantello Mfg. Co.*, 26 A. B. R. 57, 185 Fed. 276 (D. C. Me.).

^{37.} Impliedly, *Marden v. Phillips*, 4 A. B. R. 566 (D. C. Mass.); instance, *Jacobs v. Ballantine Brew. Co.*, 27 A. B. R. 918, 193 Fed. 393 (C. C. A. Mass.).

^{38.} Compare post, § 1204; also, see In *re Manistee Watch Co.*, 28 A. B. R. 316, 197 Fed. 455 (D. C. Mich.).

^{39.} In *re Kellogg*, 10 A. B. R. 7 (C. C. A. N. Y., affirming 7 A. B. R. 623), 113 Fed. 120 (D. C. N. Y., affirming 6 A. B. R. 389); In *re Miller*, 9 A. B. R. 274, 118 Fed. 360 (D. C. Ga.); In *re Wilde's Sons*, 13 A. B. R. 217 (D. C. N. Y.). Instance, *Ryttenberg v. Schefer*, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.): In this case a commission of 2½ per cent. on net sales, for guaranteeing consignments was held not usurious. Instance, In *re Sawyer*, 12 A. B. R. 269, 130 Fed. 384 (D. C. Mass.); In *re Martin*, 27 A. B. R. 151 (Ref. Tex.); instance, In *re Holmes Lumber Co.*, 26 A. B. R. 119, 189 Fed. 178 (D. C. Ala.); instance, held not usury, *Houghton v. Burden*, 228 U. S. 161, 30 A. B. R. 16.

Obiter, In re Worth, 12 A. B. R. 566, 130 Fed. 927 (D. C. Iowa): "It would seem that the legal representatives of the borrower might interpose the objection of usury the same as he might do. Whether the trustee in bankruptcy of this estate in such a representative and might interpose such objection for the purpose of preventing the allowance of illegal interest on this claim, need not be determined, for he is not interposing such objection."

In re Stern, 16 A. B. R. 510, 144 Fed. 956 (C. C. A. Iowa): "Under the Statutes of Iowa and the provisions of the Bankruptcy Act of 1898, § 57 (a), the defense of usury is as available to the debtor's trustee in bankruptcy as to the debtor himself."

But creditors may not interpose the objection, for they do not succeed to the bankrupt's personal privileges, although the trustee does so succeed.

In re Worth, 12 A. B. R. 566, 130 Fed. 927 (D. C. Iowa): "It is the settled rule in Iowa that under these sections the plea or defense of usury is personal to the borrower and cannot be interposed by a stranger to the contract. * * * The objecting creditors in the present case are in no manner parties or privies to the alleged usurious contract of the Sheldon State Bank, in no manner connected therewith, and cannot therefore be heard to interpose the objection of usury thereto."

And the burden of proof rests on the trustee pleading the usury.⁴⁰

§ 1197. May Redeem Mortgaged Property.—So, also, he may exercise the bankrupt's right to redeem mortgaged property;⁴¹ and may do so even after the creditors' time for redemption conferred by State statute had expired, if it is still within the bankrupt's statutory time, although this right usually is held to be purely personal to the debtor and not to inure to creditors.⁴²

§ 1198. May Recover Property Misapplied to Agent's Private Debt.—So, also, he may exercise the right of a principal, on the principal's discovery of the fraud, to recover property belonging to the principal that has been used by his agent with the knowledge of the agent's creditor to pay the agent's own debt.⁴³

§ 1199. May Defend That Mortgage Does Not Cover Specific After-Acquired Property or Is Void for Indefiniteness or for Failure to Comply with Statutory Requirements.—The trustee may defend that a chattel mortgage covering after-acquired property does not cover the particular after-acquired property in question;⁴⁴ or is void for

40. In re Wilde's Sons, 13 A. B. R. 217, 133 Fed. 562 (D. C. N. Y.).

41. In re Novak, 7 A. B. R. 27, 111 Fed. 161 (D. C. Iowa); In re Goldman, 4 A. B. R. 100, 102 Fed. 122 (D. C. N. Y.).

42. In re Novak, 7 A. B. R. 27, 111 Fed. 161 (D. C. Iowa).

43. In re Knox, 3 A. B. R. 371, 98 Fed. 585 (D. C. N. Y.).

44. Instance, In re Dry Dock Co., 16 A. B. R. 325, 144 Fed. 649 (C. C. A. N. Y.), wherein after-acquired material was commingled with material covered by the mortgage and all used in the construction. In re Sentenne & Green Co., 9 A. B. R. 648, 120 Fed. 436; Des Moines Nat'l Bk. v. Council B. Sav. Bk., 18 A. B. R. 108, 150 Fed. 301 (C. C. A. Iowa); Zartman v. Nat'l Bk., 16 A. B. R. 158, 109 App. Div. 406 (N. Y.);

indefiniteness;⁴⁵ or is void between the parties for failure to comply with statutory requirements.⁴⁶

The trustee may defend that a chattel mortgage claiming to cover after-acquired property contains no "after-acquired property" clause.⁴⁷

§ 1199 $\frac{1}{4}$. Or That Mortgage or Other Lien Does Not Secure Certain Obligations, etc.—The trustee may defend that a mortgage or other lien does not secure certain obligations, or that the debt secured thereby is not of the amount claimed, or is improper, etc.

Thus, he may defend against the allowance of attorney's fees to the mortgagee's attorney.

In *re Torchia*, 26 A. B. R. 188, 185 Fed. 576 (D. C. Pa.): "The objection raised before the referee to the attorney's commission on said judgments was made by the trustee and not by subsequent judgment creditors. The trustee stands in the shoes of the bankrupt. He could contest the right to the attorney's commissions had he been made a party to the proceedings in the court in which the judgments were entered. He raised the objection before the referee upon distribution at the first opportunity, and his objection should have been sustained."

§ 1200. May Urge Transfer Absolute in Form, but Mortgage in Fact.—The trustee may urge that a transfer, absolute in form, is in fact a mortgage.⁴⁸

§ 1201. May Plead Waiver.—The trustee may plead waiver;⁴⁹ as,

instance, In *re Atlanta News Pub. Co.*, 20 A. B. R. 193, 160 Fed. 519 (D. C. Ga.); instance, *Mattley v. Wolfe*, 23 A. B. R. 673, 175 Fed. 619 (D. C. Neb.), reversed on other points in *Mattley v. Geisler*, 26 A. B. R. 116, 187 Fed. 970 (C. C. A. Neb.); instance, In *re Wade*, 26 A. B. R. 169, 185 Fed. 664 (D. C. Mo.).

And where the trustee is plaintiff and seeks to recover from the mortgage property which he claims is not covered, of course the burden of proof that the property is after-acquired property not covered by the mortgage will be upon the trustee. *Mattley v. Wolfe*, 23 A. B. R. 673, 175 Fed. 619 (D. C. Neb.).

45. Instance, *Des Moines Nat'l Bk. v. Council B. Sav. Bk.*, 18 A. B. R. 108, 150 Fed. 301 (C. C. A. Iowa); *Stroud v. McDaniel*, 5 A. B. R. 695, 106 Fed. 493 (C. C. A. S. C.); impliedly, In *re Adamant Plaster Co.*, 14 A. B. R. 815, 137 Fed. 251 (D. C. N. Y.); instance held not void therefor, In *re Beede*, 11 A. B. R. 387, 120 Fed. 853 (D. C. N. Y.); instance, void where description is

"five horses" where bankrupt owned six, In *re Martin*, 23 A. B. R. 151, 173 Fed. 597 (C. C. A. Mo.).

46. Instances, held not void for indefiniteness, *Davis v. Turner*, 9 A. B. R. 704 (C. C. A. N. Car.); In *re Durham*, 8 A. B. R. 115 (D. C. Md.); In *re Berck & Co.*, 15 A. B. R. 694 (C. C. A. Ills.); instance, In *re Jules & Frederic Co.*, 27 A. B. R. 136, 193 Fed. 532 (D. C. Mass.).

47. In *re Doran*, 18 A. B. R. 760, 154 Fed. 467 (C. C. A. Ky.).

48. *Hastings v. Fithan*, 13 A. B. R. 676 (N. J. Ct. Errors); *Dulany v. Morse*, 29 A. B. R. 275 (Sup. Ct. Dist. Columbia).

49. Instance, In *re Wolf*, 3 A. B. R. 558, 98 Fed. 74 (D. C. Iowa).

Vendor under Land Contract Accepting Quit Claim Deed from Trustee Waives Claim for Purchase Price.—But this is not by virtue of his succession to the bankrupt's title but by independent right. *Kenyon v. Mulert*, 26 A. B. R. 184, 184 Fed. 824 (C. C. A. Pa.).

for instance, waiver of cash payment on delivery.⁵⁰ He may also plead waiver of a forfeiture.⁵¹

§ 1201 $\frac{1}{4}$. May Plead Abandonment.—The trustee may plead abandonment of a lien.⁵²

§ 1201 $\frac{1}{2}$. May Plead Merger.—The trustee may plead merger; as, for instance, merger of a mortgage lien in a quit claim deed.⁵³

§ 1202. May Plead Payment, Accord and Satisfaction, etc.—The trustee may plead payment or other satisfaction of a debt or lien.⁵⁴ Thus, both parties are bound by valid accord and satisfaction.⁵⁵

§ 1202 $\frac{1}{4}$. May Demand Accounting.—The trustee may demand an accounting; as, for example, where the bankrupt had previously transferred all his property to another person to sell and apply the proceeds on the claims of creditors.⁵⁶

§ 1202 $\frac{1}{2}$. May Ask Reformation of Contract.—The trustee may ask for the reformation of a contract; also he may resist such application.⁵⁷

§ 1203. Trustee Entitled to All Offsets, Rebates, etc., of Bankrupt.—The trustee is entitled to all offsets, rebates, etc., that the bankrupt would have had.⁵⁸

In *re Harper*, 23 A. B. R. 918, 175 Fed. 412 (D. C. N. Y.): "Any debt, liquidated or unliquidated, owing to the bankrupt from a creditor of his, whether for damages or on contract, express or implied, which passes to the

50. *Guarantee Title & Trust Co. v. First Nat. Bank*, 26 A. B. R. 85, 185 Fed. 373 (C. C. A. Pa.).

51. *Instance, lease, In re Montello Brick Wks.*, 20 A. B. R. 859, 163 Fed. 621 (D. C. Pa.); *instance, In re Palatable Water Co.*, 18 A. B. R. 833, 154 Fed. 531 (D. C. Pa.); *instance, land contract, Mound Mines Co. v. Hawthorne*, 23 A. B. R. 242, 173 Fed. 882 (C. C. A. Colo.).

52. *In re Hibbler*, 27 A. B. R. 612, 192 Fed. 740 (D. C. N. Y.).

53. *In re Hibbler*, 27 A. B. R. 612, 192 Fed. 740 (D. C. N. Y.).

54. *Instance, In re Thompson*, 11 A. B. R. 719, 128 Fed. 575 (C. C. A. N. Y.); compare, as to accord and satisfaction, *In re McBride & Co.*, 12 A. B. R. 31, 132 Fed. 285 (Ref. N. Y.). *Instance, Drozda v. Galbraith*, 27 A. B. R. 882, 195 Fed. 926 (C. C. A. Minn.).

55. *Instance, Missouri Elec. Co. v. Hamilton-Brown Co.*, 21 A. B. R. 270, 165 Fed. 283 (C. C. A. Mo.).

56. *Gill Trustee v. Bell's Knitting Mills*, 24 A. B. R. 275 (N. Y. App. Div.), quoted at § 1728 $\frac{1}{2}$.

57. *Impliedly, Hardy v. Chandler*, 23 A. B. R. 717, 175 Fed. 138 (D. C. Ga.).

58. See correlative right of creditor, ante subdiv. "E," of this division and chapter. *In re B. H. Douglass & Sons Co.*, 8 A. B. R. 113, 114 Fed. 772 (D. C. Conn.).

In re Royce Dry Goods Co., 13 A. B. R. 258, 133 Fed. 100 (D. C. Mo.): Off-set of deficiency of payment of subscription to stock against claim of stockholder where deficiency arises by overvaluation of property transferred in payment of stock subscriptions.

In re Brewster, 7 A. B. R. 486 (Ref. N. Y.): Advancements made to daughter after reaching her majority for money to finish her art education, offset against her claim for services to parent.

Embry v. Bennett, 20 A. B. R. 651, 162 Fed. 139 (C. C. A. Ky.): No off-set of money's expended by the bankrupt father in educating his children at college, against their claims against him for money lost by him as their guardian. See ante, § 818 $\frac{1}{2}$.

Impliedly, Powell v. U. S., 14 A. B. R. 192 (D. C. N. Y.): Rebate, internal revenue, when trustee not entitled thereto.

trustee, may, of course, be used by him to reduce the claim of such creditor when presented or to extinguish it altogether."

Thus, the trustee has been held entitled to counterclaim or offset against a creditor's claim, damages suffered by the bankrupt through the creditor's fraudulent representation inducing the entering into the contract claimed upon; and the words "mutual debts" used in § 68 (a) will include rights of action existing in favor of the bankrupt against a creditor for false representations inducing the bankrupt to enter into a contract for the sale of goods.⁵⁹ And the burden of proof is upon the trustee to establish his counterclaim,⁶⁰ since the claim itself is *prima facie* established by the deposition for proof of debt introduced in evidence by the creditor.

§ 1204. May Plead Bankrupt's Lack of Capacity and *Ultra Vires*.

—The trustee may plead the bankrupt's want of capacity under State law to become obligated.⁶¹ Thus, the trustee may plead that a transfer was *ultra vires*.^{61a}

American Mach. Co. v. Norment, 19 A. B. R. 679, 157 Fed. 801 (C. C. A. N. Car.): "Again, the misappropriation of these 17 \$1,000 notes secured by this deed of trust executed by this bankrupt corporation, by its managing officer, to his own use, to the security of his own debt, is so clear and apparent, that such act must be held clearly unauthorized and beyond the scope of his power or right as such officer. To hold otherwise would establish the dangerous doctrine that a managing officer of a corporation, having possession of its notes and securities, could dispose of them at will. Finally, it is clear that an attempt upon the part of even a majority of stockholders to divert the corporation assets to purposes wholly outside of the scope of its charter powers, purposes that clearly can inure to no benefit to it or its stockholders and creditors as such, is *ultra vires* and void. We therefore, for these reasons, find no error in the ruling of the court below that the notes and deed of trust executed by the bankrupt corporation are void as against its creditors."

But it has been held, that corporate officers, assuming to act as directors, with the stockholders' acquiescence, will bind the corporation bankrupt.⁶²

§ 1205. May Urge Articles Not Fixtures.—And the trustee succeeds to the bankrupt's rights to urge that articles, such as machinery, etc., have not become fixtures but still belong to the bankrupt estate.⁶³

⁵⁹. In re Harper, 23 A. B. R. 918, 175 Fed. 412 (D. C. N. Y.).

⁶⁰. In re Harper, 23 A. B. R. 918, 175 Fed. 412 (D. C. N. Y.).

⁶¹. Instance, In re Smith Lumber Co., 13 A. B. R. 118, 132 Fed. 618 (D. C. Tex.): *Ultra vires* guaranty by a corporation, bankrupt.

Instance, *Cunningham v. Germ. Ins. Bk.*, 4 A. B. R. 363, 101 Fed. 977 (C. C. A. Ky.): Indebtedness of bankrupt corporation alleged to be in excess of charter limits yet held binding on the facts.

^{61a}. Compare ante, § 1195; also,

In re Manistee Watch Co., 28 A. B. R. 316, 197 Fed. 455 (D. C. Mich.).

⁶². *Cunningham v. Germ. Ins. Bk.*, 4 A. B. R. 363, 101 Fed. 977 (C. C. A. Ky.): Executive officers assuming functions of board of directors, by acquiescence of stockholders, bind bankrupt corporation.

⁶³. In re Rodgers & Hite, 16 A. B. R. 401 (D. C. Pa.). See ante, § 1152.

Instance, brick making plant-kilns, factory building, engines, boilers, etc., held removable trade fixtures. In re Montello Brick Works, 20 A. B. R. 859, 163 Fed. 621 (D. C. Pa.). Possibly, in-

§ 1206. **May Urge Facts Constitute Sale.**—The trustee may urge that the facts constituted a sale to the bankrupt.⁶⁴ Thus, the trustee may urge that the title to goods sold to the bankrupt on approval has passed by long delay.⁶⁵

§ 1206 $\frac{1}{4}$. **Or Novation.**—And the trustee may urge that the facts constitute a novation.⁶⁶

§ 1206 $\frac{1}{2}$. **May Urge Facts Do Not Constitute Pledge or Other Transfer.**—The trustee may defend that there has not been a sufficient delivery or that there are other essentials lacking which would be requisite to effect a transfer of title by way of pledge or otherwise.⁶⁷

The trustee may urge that an apparent delivery was not intended as a final transfer of title until recording.⁶⁸

DIVISION 2.

RIGHTS OF TRUSTEE AS SUCCESSOR TO RIGHTS OF CREDITORS UNDER STATE LAW.

§ 1207. **Second, Trustee's Title and Rights as Successor to Creditors under State Law.**—The Amendment of 1910 to Bankruptcy

stance, *In re Darlington*, 20 A. B. R. 805, 163 Fed. 389 (D. C. N. Y.); instance, turpentine still, not machinery. *In re Anderson*, 21 A. B. R. 413 (Ref. Ga.); instance, steam shovel, *In re Montello Brick Works*, supra.

64. See correlative subject of taking title subject to bankrupt's sales, etc., ante, § 1145, et seq.

65. *In re Paper Co.*, 17 A. B. R. 121, 147 Fed. 858 (D. C. Penn.).

Other Instances of Defenses of Bankrupt to Which Trustee Succeeds.—Parol evidence to vary written lease: the trustee has the same right as the bankrupt to demand that a written lease be not varied except on clear and satisfying evidence. *In re Luckenbill*, 11 A. B. R. 455, 127 Fed. 984 (D. C. Pa.).

Parol Evidence to Show What Future Advances Intended.—Where a valid real estate mortgage was given to cover future advances, the court held parol evidence incompetent to show the parties intended it to cover advances for other purposes than the protection of the mortgage lien. *Hendricks v. Webster*, 20 A. B. R. 112, 159 Fed. 927 (C. C. A. Iowa).

Trustee of bankrupt heir may contest account of administrator. The trustee of a bankrupt heir may contest the account of the administrator. *In re Clute*, 2 A. B. R. 376 (Super. Court San Francisco). Even though the bankrupt himself be the administrator.

Trustee may recover part payment on bankrupt's oral contract for the purchase of land where the seller has refused to make a deed to the trustee and has leased the land to another. *Durham v. Wick*, 14 A. B. R. 385, 210 Pa. St. 128.

Vendor of land under land contract, accepting quit claim deed from trustee loses claim for purchase price. *Kenny v. Muler*, 26 A. B. R. 184, 184 Fed. 825 (C. C. A. Pa.). But this is not by virtue of succeeding to the bankrupt's rights but as an independent right more properly considered ante, § 932, as a right to abandon burdensome assets.

66. Instance, *Long v. Gump*, 16 A. B. R. 501, 144 Fed. 824 (C. C. A. Ohio); instance, novation, however, found not to exist, *In re Straub*, 19 A. B. R. 808, 158 Fed. 375 (D. C. W. Va.).

What Constitutes Novation.—Reorganized corporation, composed of directors and bondholders, buying in insolvent's assets and accepting bonds, and stocks, do not thereby make novation. *In re Medina Quarry Co.*, 24 A. B. R. 769, 179 Fed. 929 (D. C. N. Y.).

67. *French v. White*, 18 A. B. R. 905, 78 Vt. 89; also, *In re Automobile Liv- erty Service Co.*, 23 A. B. R. 799, 176 Fed. 792 (D. C. Ala.). Compare ante, § 1146, et seq.

68. Compare to this effect, *Ragan v. Donovan*, 26 A. B. R. 311, 189 Fed. 138 (D. C. Ohio), quoted at § 1334 $\frac{1}{4}$.

Act, § 47a (2), provides that the trustee, as to all property in the custody or coming into the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon, and also as to all property not in the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies and powers of a judgment creditor holding an execution duly returned unsatisfied. This amendment, whilst still preserving to the trustee all the rights, remedies and powers of the bankrupt, as given in the Bankruptcy Act, § 70, no longer limits him to those rights, but effectually lifts him out of his former contracted position "in the shoes of the bankrupt," and gives to him the rights also of a creditor "armed with process" so that, as previously remarked, in § 1137 et seq., the trustee's title is enlarged, and, instead of being merely the successor to the bankrupt's title, with, of course the peculiar rights conferred by the Bankruptcy Act relative to preferences, etc., and the very limited additional rights of any existing creditor (in some States only if such creditor be "armed with process"), it now includes also whatever rights creditors under State law would have had had they been "armed with process," whether actually so "armed" or not; the trustee being deemed a levying creditor, so far as property in the custody of the bankruptcy court is concerned, and a creditor armed with an execution returned unsatisfied as to property not in such custody.

By this amendment the discussions of §§ 1208, 1209, 1210, 1211, 1212, 1213, 1214, of the first edition of this treatise are displaced, although they are still instructive as explaining the meaning of the Amendment of 1910 in this particular, as well as showing the reasonings of the courts in adopting the former doctrine, and they are accordingly given in substance in the notes to § 1270 together with all later decisions rendered under the law as it stood before the Amendment.

A full discussion of the changes effected by the Amendment of 1910 in the title of the trustee is had, ante, in § 1137 et seq. In accordance with the rules therein enunciated the statement of the trustee's title and rights as successor to the creditors is now as follows, to-wit:

In cases affected by the fraud of the bankrupt towards creditors, as also where there has been some transfer, encumbrance, or holding of the property void as to the bankrupt's creditors or inuring to their benefit by State law, for want of record or otherwise, the trustee succeeds to the rights of any existing creditor already qualified by State law; and, also, as to the property in the custody or coming into the custody of the bankruptcy court, the trustee is to be deemed vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon, and, as to the property not in such custody, is to be deemed vested, as of the date of the filing of the bankruptcy petition, with all the rights, remedies and powers of a judgment creditor holding an execution duly returned unsatisfied.

§ 1208. Trustee's Title and Rights as Successor to Creditors a Three-Fold Subject.—Not only is it true that the title of the trustee is three fold, namely that he takes first the title of the bankrupt, second the title of creditors under state law, and third the peculiar rights conferred by the bankruptcy act to set aside preferential transfers and liens by legal proceedings acquired within four months of the bankruptcy, but it is also to be noted that the second title of the trustee, namely, that which he derives under state law from creditors, is itself a three-fold subject. Thus, as to the trustee's rights as successor to creditors under state law, the trustee has the right to set aside fraudulent transfers and to recover property fraudulently held, this right being guaranteed by § 70 (a) (4), § 70 (e) and § 67 (e) of the Bankruptcy Act; second, he is subrogated to, or clothed with, the rights of any existing creditor as to whom any transaction is voidable, such right being guaranteed to him by § 67 (a), (b), (e) and, as to subrogation, (f) of the Bankruptcy Act; third, the trustee is, by the Amendment of 1910 to the Bankruptcy Act, § 47 (a) (2), to be deemed a creditor under state law "armed with process," whether or not, in fact, there be such a creditor actually in existence.

It must, therefore, not be overlooked that the Amendment of 1910 to § 47 (a) 2 of the Act, whereby the trustee is virtually made a creditor "armed with process," does not express all the rights and title of the trustee which he has under local law. For example, the rights he has under the Amendment of 1910 would not antedate the filing of the bankruptcy petition. So, for example, there might be cases where liens were not recorded for a time and yet were ultimately recorded before the filing of the bankruptcy petition. These liens, in most states, would nevertheless be valid and so would not be affected by the Amendment. Yet they could be avoided by the trustee, if, during the period that they were not recorded and within four months of the filing of the bankruptcy petition, some creditor had obtained a lien by legal proceedings thereon, since by Bankruptcy Act, § 67, the trustee would be subrogated to and could enforce the rights of such creditor. Again, as to fraudulently transferred property, or property held under fraudulent trust, the trustee would have right and title thereto, even were it not for the Amendment of 1910, such right and title being given to him by §§ 70 (a) (4), 70 (e) and 67 (e) and in some respects by §§ 67 (a) and 67 (b) these latter sections being aided as to some transactions by the subrogation of liens for the benefit of the estate provided for in § 67 (f).

So the trustee's second title which we are now about to consider—his title as a creditor, or as the successor to creditors, under state law—naturally divides itself into the following sub-heads:

Rights as to fraudulent transfers and holdings, under § 70 (a) (4) and § 70 (e) and § 67 (e).

Rights which some existing creditor actually has acquired and to which

the trustee is subrogated under § 67 (a), (b) and (c) as aided by the provisions of § 67 (f) for the preservation for the benefit of the bankrupt estate of otherwise nullified liens.

Rights which are independently conferred by the Amendment of 1910 to § 47 (a) (2) whereby he is to be deemed vested with the rights of a creditor under state law "armed with process."⁶⁹

We will take up these sub-heads in their order.

SUBDIVISION "A."

FRAUDULENT TRANSFERS AND PROPERTY HELD ON FRAUDULENT TRUSTS.

§ 1209. Fraudulently Transferred Property Recoverable.—As to property "affected by the bankrupt's fraud towards creditors," as we have seen in preceding sections [§§ 1137, et seq., 1207, 1208], the title taken by

69. Bankr. Act, § 70 (a) 4: "The trustee shall be vested by operation of law with the title of the bankrupt * * * to all * * * (4) property transferred by him in fraud of his creditors."

Bankr. Act, § 70 (e): "The trustee may avoid any transfer by the bankrupt of his property which any creditor of such bankrupt might have avoided, and may recover the property so transferred, unless he was a bona fide holder for value, prior to the date of the adjudication. Such property may be recovered or its value collected from whoever may have received it, except a bona fide holder for value."

Bankr. Act, § 67 (a): "Claims which for want of record or for other reasons would not have been valid liens as against the claims of the creditor of the bankrupt shall not be liens against his estate."

Bankr. Act, § 67 (b): "Whenever a creditor is prevented from enforcing his rights as against a lien created, or attempted to be created, by his debtor, who afterwards becomes a bankrupt, the trustee of the estate of such bankrupt shall be subrogated to and may enforce such rights of such creditor for the benefit of the estate."

Bankr. Act, § 67 (e): "And all conveyances, transfers or incumbrances of his property made by a debtor at any time within four months prior to the filing of the petition against him, and while insolvent, which are held null and void as against the creditors of such debtor by the laws of the State, Territory, or District in which such property is situate, shall be deemed null and void under this act against the creditors of such debtor if he be adjudged a bankrupt, and such prop-

erty shall pass to the assignee [trustee] and be by him reclaimed and recovered for the benefit of the creditors of the bankrupt."

Bankr. Act, § 67 (f) in its latter clauses provides for the trustee's subrogation to liens of creditors obtained by legal proceedings within four months of the bankruptcy and which are therefore null and void under the earlier clause of the section as against the trustee, but as to which some prior transfer or lien upon the property would be itself rendered void under State law though good as to the trustee. Thus § 67 (f) in its earlier clauses "prevent" to use the words of § 67 (f) "the creditor from enforcing his rights as against" the prior transfer or encumbrance, but in its latter clause preserves the lien for the benefit of the estate, this latter clause reading " * * * unless the court shall, on due notice, order the right under such levy, judgment, attachment or other lien shall be preserved for the benefit of the estate; and thereupon the same may pass to and shall be preserved by the trustee for the benefit of the estate as aforesaid."

Bankr. Act, § 47 (a) (2) as Amended in 1910: "and such trustees, as to all property in the custody or coming into the custody of the bankruptcy court shall be deemed vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon; and also, as to all property not in the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies and powers of a judgment creditor holding an execution duly returned unsatisfied."

the trustee, at no time in the history of the bankruptcy law, has been necessarily that of creditors "armed with process," much less that of the bankrupt himself. As to such property he neither "stands in the shoes of the bankrupt" nor requires "arming with process." To property transferred fraudulently by the bankrupt, the Bankruptcy Act, from its first enactment, always has given direct title to the trustee, in § 70 (a) (4); whilst as to property not "transferred" by the bankrupt, but otherwise held by him or for him in fraud of creditors, the uniform exception in the Supreme Court's decisions, which have stated the rule as to standing "in the bankrupt's shoes" always with the qualification that the trustee so stands only "in cases unaffected by the fraud of the bankrupt towards creditors," disposes, similarly, of the necessity of the existence of creditors "armed with process;" so that the creditor's title taken in cases of fraud has always been fundamentally different from what it has been in other cases where the creditor's title is taken, in other cases the trustee getting (until the Amendment of 1910 gave him better rights) only such title as already had been actually asserted by some creditor.

Property, then, which, according to the state law, has been fraudulently transferred is recoverable by the trustee and the fraudulent transaction may be set aside.⁷⁰

Security Warehousing Co. v. Hand, 19 A. B. R. 291, 206 U. S. 415: "* * * and it is contended that the transfers were valid between the parties; that the

70. Bankr. Act, §§ 70 (a) (4); 70 (e); also § 67 (e) last part. Also compare post, § 1493, et seq. and § 1709.

For pleadings and practice in actions by trustee to set aside fraudulent conveyances, see post, "Pleadings and Practice in Actions by Trustees," ch. XXXIII, div. 4, subdiv. "A."

Cases of fraudulent conveyances under Act 1 of acts of bankruptcy are in point here, see ante, § 104, et seq.

Barker v. Franklin, 8 A. B. R. 468 (Sup. Ct. N. Y.); *Small v. Muller*, 8 A. B. R. 448 (Sup. Ct. N. Y. App. Div.); *In re Grohs*, 1 A. B. R. 465 (Ref. Ohio); *In re Mullen*, 4 A. B. R. 224, 101 Fed. 413 (D. C. Mass.); *Schmidt v. Dahl*, 11 A. B. R. 226 (Minn. Sup. Ct.), in which case, however, there had been, previously to bankruptcy, a judgment obtained by a creditor. *Johnston v. Forsyth Mercantile Co.*, 11 A. B. R. 669, 127 Fed. 845 (D. C. Ga.); instance, *Hosmer v. Tiffany*, 17 A. B. R. 318, 115 App. Div. (N. Y.) 303; *Evans v. Staalle*, 11 A. B. R. 182, 92 N. W. 951 (Minn.). In addition, *Coder v. Arts*, 22 A. B. R. 1, 213 U. S. 223, quoted in part at § 1498; *Allen v. Gray*, 21 A. B. R. 828 (N. Y. Sup. Ct.); *Phillips Tr. v. Kleinman*, 23 A. B. R. 266 (Pa. Com.

Pleas); (*Security Warehousing Co. v. Hand*, 19 A. B. R. 291, 206 U. S. 415, quoted at § 1139; (1867) *Bean v. Am-sink*, 8 N. B. Reg. 228.

Other instances of fraudulently conveyed property being held recoverable by the trustee:

1. Conveyance to daughter. *Schmitt v. Dahl*, 11 A. B. R. 226 (Sup. Ct. Minn.).

2. Conveyance to sister. *Durack v. Wilson*, 13 A. B. R. 774 (N. Y. Sup. Ct.).

3. A claim for money paid to the bankrupt on an alleged sale and transfer of goods at a time when he was insolvent to the knowledge of the purchaser, under circumstances tending to show the alleged transfer was a scheme to hinder and defraud creditors, held properly rejected although the goods had been sold by the trustee. *In re Lansaw*, 9 A. B. R. 167, 118 Fed. 365 (D. C. Mo.).

4. A firm apparently solvent suddenly determines to call itself insolvent, confesses judgments and transfers its accounts to favorite creditors, has a friendly receiver collusively appointed, conveys all individual real estate to a favored creditor and thus puts

trustee in bankruptcy takes only the title and right of the bankrupt and therefore he cannot assert a right not possessed by the knitting company. It is no new doctrine that the assignee or trustee in bankruptcy stands in the shoes of the bankrupt and that the property in his hands, unless otherwise provided by the Bankrupt Act, is subject to all of the equities impressed upon it in the hands of the bankrupt. This has been the rule under former acts and is now the rule * * * By § 70 (a) the trustee in bankruptcy is vested, by operation of law, with the title of the bankrupt to all property transferred by operation of law, with the title of the bankrupt to all property transferred by him in fraud of his creditors, and to all property which prior to the filing of the petition might have been levied on and sold by judicial process against him; and by subdivision (e) of the same section, the trustee in bankruptcy may avoid any transfer by the bankrupt of his property which any creditor of the bankrupt might avoid, and may recover the property so transferred or its value. Here are special provisions placing the title of the property transferred by fraud or otherwise, as mentioned, in the trustee in bankruptcy, and giving him the power to avoid the same. * * * The case illustrates the distinction taken between fraud in fact and the mere failure to file a mortgage otherwise valid against the world."

Bush v. Export Storage Co., 14 A. B. R. 141, 136 Fed. 918 (C. C. Tenn.): "But besides this class of transfers made void by the Bankrupt Act itself, as being against its policy of equal and fair distribution the bankruptcy law (§ 70a,

all its visible assets beyond the reach of unsecured creditors. *Barker v. Franklin*, 8 A. B. R. 468.

5. Bankrupt buying costly furniture and giving it to his bride as fast as bought. *Hosmer v. Tiffany*, 17 A. B. R. 318, 115 App. Div. (N. Y.) 303.

6. Payment of wife's mortgage. *In re Bartheleme*, 11 A. B. R. 67 (Ref. N. Y.).

7. Chattel mortgage and bill of sale. *Small v. Muller*, 8 A. B. R. 448 (N. Y. Sup. Ct. App. Div.).

8. Bankrupt had arranged with a storage company having no warehouse of its own, to issue to him warehouse receipts on his own goods purchased by him on credit and stored in his own warehouse on his own premises, with evident marks of design to deceive those dealing with him into the belief that the property was his own without notice of the secret lien of third parties to whom the warehouse receipts were pledged or sold; in which case the court held the trustee would take the creditors' rights and the subterfuge would not avail. *In re Rodgers*, 11 A. B. R. 79, 125 Fed. 169 (C. C. A. Ills., reversed, but on other grounds, sub nom. *B'k v. Title Trust Co.*, 198 U. S. 280, 14 A. B. R. 102).

9. Transferring practically all available property to relatives by different transfers, all within a week, *Horner-Gaylord Co. v. Miller & Bennett Co.*, 17 A. B. R. 267, 147 Fed. 295 (D. C. W. Va.).

10. Composition with creditors be-

fore bankruptcy, with a secret preference to one, although secret preference is given more than four months before bankruptcy, void under general equity principles as against creditors as being, 1st, an oppression of the debtor; and 2d, a fraud of the other creditor. *In re Chaplin*, 8 A. B. R. 121 (D. C. Mass.).

11. Relinquishment of dower as consideration for transfer. *Moore v. Green*, 16 A. B. R. 648 (C. C. A. W. Va., reversing *In re Porterfield*, 15 A. B. R. 11).

12. Fictitious sale by bankrupt shortly prior to bankruptcy. *In re Siegel*, 21 A. B. R. 154, 164 Fed. 559 (D. C. N. Y.).

13. Real estate purchased partly with funds derived from a boarding house run by wife, but deed not delivered until eve of bankruptcy, and clear intent shown to aid husband to get goods on credit on false appearances. *Prescott v. Gallussio*, 21 A. B. R. 229, 164 Fed. 618 (D. C. N. Y.).

14. Peculiar case; wherein it was held that the trustee was subrogated to the rights of certain sellers who had sold their goods to the bankrupt through fraudulent misrepresentations, to pursue the property into the hands of third parties to whom in turn the bankrupt had transferred them with full knowledge of the fraud, the defrauded sellers themselves having waived the fraud by proving their claims in bankruptcy. *Lynch v. Bronson*, 20 A. B. R. 409, 160 Fed. 139 (D. C. Conn.). But this decision does not

subsec. 4, 30 Stat. 566), provides that the trustee shall be vested by operation of law with any property transferred by the bankrupt in fraud of his creditors, the precise language of the Act being 'transferred by him in fraud of his creditors.' There is no four months limitation on this class of transfers, and this provision includes fraudulent conveyances which are so by the common law, by statute law, and by any other recognized rule of law of the State. Of course, the fraudulent bankrupt is without right to set aside a conveyance made by him in fraud of his creditors. It is valid between the parties, but, by operation of the very terms of the Act, the right which before bankruptcy belonged to the creditors passed from them, and is vested in the trustee."

Beasley v. Coggins, 12 A. B. R. 355, 48 Fla. 215, 57 So. Rep. 213: "Section 70 (e) was intended to provide simply that the trustee in bankruptcy should have the same right to avoid conveyances as was possessed by creditors, or any of them, and this with especial reference to the statute of 13 Elizabeth. Under the Bankruptcy Act, when one is thereunder adjudged a bankrupt, creditors are not permitted to attack fraudulent conveyances of their debtor, made more than four months of the adjudication of bankruptcy; and, if the trustee could not do so, then the act would constitute 'a device to permit fraudulent conveyances to take effect with impunity in case they are successfully concealed for the specified four months.' *Lewis v. Bishop*, 47 App. Div. 554, text, 558, 62 N. Y. Supp. 618. It is only by holding that the trustee is subrogated to the

seem to state sound law, for it would seem that the right of such creditors was to have pursued the property themselves and that by waiving the right they did not confer it on the trustee, but that the trustee was relegated to such right as all the creditors possessed, not to those of the defrauded sellers who had sold to the bankrupt, whose fraud did not harm the estate but only the sellers themselves.

15. Depositing funds in fictitious names assisted by his attorney. *Clay v. Waters*, 20 A. B. R. 561, 161 Fed. 815 (C. C. A. Mo.).

16. Country merchant transferring to banker all his property at 75 per cent. of its true value, no inventory, mere cursory examination, no inquiry about indebtedness, knowledge of dishonored checks within forty days. *Houck v. Christy*, 18 A. B. R. 330, 152 Fed. 612 (C. C. A. Kans.).

17. Unfiled bill of sale of sewing machines, where dates of instruments false, etc. In re *Schlessel*, 18 A. B. R. 434 (Ref. N. Y.).

18. Sale of entire stock two days before bankruptcy, effected behind closed doors, part of proceeds paid over to preferred creditors, though sale based on presently passing consideration. *Johnston v. Forsyth Mercantile Co.*, 19 A. B. R. 48 (D. C. Ga.).

19. Sale of entire stock of goods of retail merchant casts burden of proof on purchaser, when. *Allen v. McMannes*, 19 A. B. R. 276, 156 Fed. 615 (D. C. Wis.).

20. Pretended "warehousing" and pledge though debtor continued still to use the goods. (*Security*) *Warehousing Co. v. Hand*, 19 A. B. R. 291, 206 U. S. 415, quoted at § 1139; *Fourth St. Nat. Bank v. Millbourne Mills Co.*, 22 A. B. R. 442, 172 Fed. 177 (C. C. A. Pa.).

21. Voluntary transfers to wives within the four months, held void under § 67 (e), but whether voidable only under the first provision of § 67 (e) not adverted to. *Henkel v. Seider*, 20 A. B. R. 773, 163 Fed. 553 (D. C. N. Y.).

22. Pretended sale of real estate. *Visanska v. Cohen*, 21 A. B. R. 350, 165 Fed. 552 (D. C. Ga.).

23. Forming corporation to take over assets of an insolvent debtor for the purpose of defeating his creditors, assets thus sold held still to belong to bankrupt seller's estate. In re (*Holbrook*) *Shoe & Leather Co.*, 21 A. B. R. 511, 165 Fed. 973 (D. C. Mont.).

24. One creditor receiving secret advantage over others in a composition, amount paid recoverable by trustee. (1867) *Bean v. Amsink*, 8 N. B. Reg. 228.

25. Pretended pledging of books by a publishing concern where debtor continues to exercise dominion. In re *Gebbie*, 21 A. B. R. 694, 176 Fed. 609 (D. C. Pa.).

26. Pretended consignments, etc. See post, § 1228, et seq.

27. Conveyance of real estate two years before bankruptcy, without consideration, conveyance itself creating the insolvency. *Phillips Tr. v. Klein-*

rights of creditors against a fraudulent conveyance that full effect and operation can be given to the statute of 13 Elizabeth against fraudulent conveyances, from which our statute (§ 1991, Rev. St. 1892) is substantially taken. * * *

"A trustee in bankruptcy occupies a relation similar to that of a judgment creditor of the bankrupt, and may file a bill in equity to set aside a fraudulent conveyance of real estate by the bankrupt, although neither the trustee nor any creditor has reduced any claim against the bankrupt to judgment."

Am. Mach. Co. v. Norment, 19 A. B. R. 679, 157 Fed. 801 (C. C. A. B. N. Car.): "But again we must go a step farther. For these parties to secure from this insolvent lumber company this deed of trust, sufficient to consume the sum total of its assets, to secure debts not its own, but personal ones alone of its principal stockholder and manager; debts of his incurred before its corporate birth, not one dollar of which, so far as shown, it derived any benefit of—not only stamps the transaction outside of the saving subdivision 'd' of § 67 of the act, but clearly brings it within the scope of subdivision 'e' of that section. It must be held a clear fraud upon the rights of creditors, and both the deed of trust and the debt itself must be held void as to such creditors."

In *re Carpenter*, 11 A. B. R. 147, 125 Fed. 831 (D. C. N. Y.): "The trustee in bankruptcy may take advantage of the invalidity of this instrument the same as a judgment creditor. It is not such a case as *In re N. Y. Economical Ptg. Co.*, 6 A. B. R. 615, 110 Fed. 514. As a mortgage it is void as against all

man, 23 A. B. R. 266 (Pa. Com. Pleas).

28. Deed of real estate from wife to husband on eve of bankruptcy of firm of which both were partners, held prima facie fraudulent where grantor has nothing left with which to pay creditors. *Fouche v. Shearer*, 22 A. B. R. 828, 172 Fed. 592 (D. C. Ga.).

29. Japanese merchant in failing condition, warning fellow countrymen so that they get pay in full whilst others wait, held not only preferential transfer but also transfer to hinder and delay other creditors, under Bankruptcy Act, § 67 (e). *Spencer v. Nekemoto*, 24 A. B. R. 517 (D. C. Hawaii.).

30. Insolvent corporation selling out assets to reorganized corporation pursuant to plan of bondholders and directors, held to hinder, delay and defraud. In *re Medina Quarry Co.*, 24 A. B. R. 769, 182 Fed. 508 (D. C. N. Y.); similarly, In *re [Holbrook] Shoe & Leather Co.*, 21 A. B. R. 511, 165 Fed. 973 (D. C. Mont.).

31. Mortgage of entire stock of goods. *Lumpkins v. Foley*, 29 A. B. R. 673, 204 Fed. 372 (C. C. A. Ga.).

Other instances, in some of which the facts have been held insufficient for recovery:

1. In *re Little River Lumber Co.*, 1 A. B. R. 482, 92 Fed. 585 (D. C. Ark.), affirmed in 4 A. B. R. 313.

2. *Jacobs v. Van Sickel*, 10 A. B. R. 519, 123 Fed. 340 (C. C. A. N. J.), affirmed in 11 A. B. R. 470, 127 Fed. 62.

3. *Pratt v. Christie*, 12 A. B. R. 1, 95 App. Div. (N. Y.) 282.

4. *Hackney v. First Nat'l Bank*, 11 A. B. R. 240, 68 Neb. 594.

5. *Fowler v. Jenks*, 11 A. B. R. 255, 90 Minn. 74 (Minn.).

6. Bankrupts, commission merchants, by contract do all their commission business in the name of another firm of commission merchants to whom the bankrupts' lease is assigned and who guarantee the consignments and receive a commission for so doing; but the bankrupts continue to occupy the leasehold and attend to the actual management of the business; the other firm claiming, on bankruptcy, to have a factor's lien for advances on the property in the bankrupt's possession; held, not to be a fraudulent device to hinder creditors. *Ryttenberg v. Schefer*, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.).

7. An action, by a purchaser from the trustee, who had purchased the trustee's interest in certain contracts securing commissions as insurance agent which the bankrupt had transferred to his wife. The purchaser recovered on the ground of its being a preference but was refused relief on the other ground of fraudulent conveyance. *Bryan v. Madden*, 11 A. B. R. 763, 78 N. Y. Supp. 230.

8. One partner of an insolvent firm selling out to the other operates to hinder and delay firm creditors and to subordinate their rights in the partnership assets to the claims of the indi-

creditors, because made in fraud of creditors. Section 70 of the Bankruptcy Act says that, not because of the omission to file or refile."

Andrews v. Mather, 9 A. B. R. 296, 134 Ala. 358: "Although property which has been fraudulently conveyed ceases to belong to the grantor, so far as any claim he himself can set up is concerned, yet the law regards property which has been fraudulently conveyed, as still the property of the grantor, so far as creditors are concerned. The assignee in bankruptcy is an officer created for the benefit of creditors, and he is permitted to regard property fraudulently conveyed in the same way in which creditors are permitted to regard it."

Mitchell v. Mitchell, 17 A. B. R. 389 (D. C. N. Car.): "A trustee in bankruptcy may avoid a mortgage fraudulent under a bankrupt law. The title attempted to be passed by such mortgage vests in such trustee. He stands in the shoes of the bankrupt, but represents the creditors, and is entitled to possession, and may bring an action to enforce his right of possession. He can maintain any action either could maintain. Such an action is not analogous to a creditor's bill, and it is no objection to it that the claims against the bankrupt are not in judgment. The title is vested in him by operation of law.

"The bankrupt law instead of vesting in the trustee the remedies of the creditors against the property judgment, execution and creditor's bills [but since

vidual creditors of the remaining partner. In *re Head & Smith*, 7 A. B. R. 556, 114 Fed. 489 (D. C. Ark.).

9. Property reconveyed to bankrupt by fraudulent grantee before petition in bankruptcy filed vests in trustee notwithstanding custody of State court receiver in suit to set aside the original conveyance, since the reconveyance divests the receiver. In *re Brown*, 1 A. B. R. 107 (D. C. Ore.).

10. Held not sufficient proof of fraud, *Allen v. Gray*, 24 A. B. R. 642, 123 App. Div. N. Y. S. 1104.

11. Chattel mortgage given for more than actual consideration, though actual consideration "presently passing." In *re Mahland*, 26 A. B. R. 81, 184 Fed. 743 (D. C. N. Y.).

12. Agreement to accept personal services and support as pay for notes, no new consideration being given therefor, is void against the trustee. In *re Powers*, 1 A. B. R. 432 (Ref. Vt.).

13. Bill of sale of all property, while insolvent, to wife and all future reacquired property for five years. In *re Hemstreet*, 14 A. B. R. 823 (D. C. Iowa).

14. In *re Porterfield*, 15 A. B. R. 11, 138 Fed. 192 (D. C. W. Va., reversed sub nom. *Moore v. Green*, 16 A. B. R. 648).

15. Third persons innocent of fraud are not proper parties. *North, Trustee v. Taylor*, 6 A. B. R. 233, 61 App. Div. 253, 70 N. Y. Supp. 338.

16. Wife's equitable interest in farm purchased jointly with her funds, but contract of purchase or bond for

title taken in husband's name alone without her consent but finally acquiesced in on promise that deed should be jointly to her when executed; held, not to estop wife as against general creditors. In *re Garner*, 6 A. B. R. 596 (D. C. Ga.).

17. *Bryan v. Madden*, 11 A. B. R. 763, 78 N. Y. Supp. 220. This was an action, however, by a purchaser from the trustee, who had purchased the trustee's interest in certain contracts securing commissions as insurance agent which the bankrupt had transferred to his wife. The purchaser recovered on the ground of its being a conveyance, but was refused relief on the other ground of fraudulent conveyance.

18. Creditors organize corporation to take over all assets; the corporation itself goes into bankruptcy but not the original debtor; transfer to the corporation is not fraudulent. In *re Robert Shaw Mfg. Co.*, 13 A. B. R. 409, 133 Fed. 556 (D. C. Penn.).

19. Partners building, each, a home on property owned in common; after dissolution of firm and before bankruptcy of one partner, each house with half of land conveyed to respective wives; but no settlement of partnership affairs ever made, no proper books kept, etc., and facts too indefinite. *Ludvig v. Umstadtter*, 17 A. B. R. 774 (D. C. N. Y.).

20. Sale in bulk but purchaser innocent, and purchase price paid out to creditors, not set aside. *Gorham v. Buzzell*, 24 A. B. R. 440, 178 Fed. 596 (D. C. Me.). Similarly, In *re Mel-*

Amendment of 1910 the trustee does have such rights] vests in him at once the title to the property—makes him the owner.

"It is argued that the mortgage in controversy being good as between the parties is also good as between the mortgagees and trustee in bankruptcy of the mortgagor; but the rule is well settled that the trustee represents the rights of creditors, and may attack conveyances made by the bankrupt in fraud of creditors. It is so provided in the statute. The trustee may prosecute any suit to recover assets in the hands of third parties, or to enforce the payment of claims that could have been prosecuted by the creditors themselves had no proceedings in bankruptcy been instituted."

In *re Gebbie & Co.*, 21 A. B. R. 691, 167 Fed. 609 (D. C. Pa.): "As it seems to me the superiority of the trustee's title is clear. In some cases he merely stands in the bankrupt's shoes, but his position here is different because the bankruptcy act expressly gives him a better title and therefore the doctrine of *York Mfg. Co. v. Cassell*, 201 U. S. 344, 15 A. B. R. 635, does not apply."

In *re Rodgers*, 11 A. B. R. 93, 125 Fed. 169 (C. C. A. Ills. reversed, on ground that summary jurisdiction did not exist, sub nom. *Bank v. Title & Trust Co.*, 14 A. B. R. 102, 198 U. S. 280): "We are therefore brought to the question whether, under the Bankruptcy Law, the trustee takes solely in the right of the bankrupt, or whether he also represents the rights which creditors have, and the authority to enforce them; whether the petition in bankruptcy is merely the appropriation by the bankrupt of his property to his creditors, or an assertion in behalf of creditors of rights which they had independently of the bankrupt, and which he himself could not assert. Notwithstanding some loose expression in the decisions upon this subject, we are satisfied, from a careful scrutiny of

ina Quarry Co., 24 A. B. R. 769, 182 Fed. 508 (D. C. N. Y.).

21. Sale of entire stock of merchandise and fixtures in bulk, but purchaser innocent of participation in seller's fraudulent intent, sale not set aside. *Shelton, Trustee v. Price*, 23 A. B. R. 431, 174 Fed. 891 (D. C. Ala.).

22. Partner selling out all the firm assets to remaining partner although both partners and firm also insolvent, not per se fraudulent. *Sargent v. Blake*, 20 A. B. R. 115, 160 Fed. 57 (C. C. A. Mo.).

23. Insolvent partnership paying individual debt of one partner, not per se fraudulent. *Sargent v. Blake*, 20 A. B. R. 115, 160 Fed. 57 (C. C. A. Mo.).

24. Bill of sale of machinery by bankrupt corporation to secure its principal stockholder for trust funds illegally turned over to it by her, the machinery remaining in possession of the corporation as "under lease." In *re Arkonia Fabric Mfg. Co.*, 18 A. B. R. 470, 151 Fed. 914 (D. C. Pa.).

25. Where, anterior to the four months period, a bankrupt, while insolvent, transfers to his wife for a nominal consideration all of his attachable property, consisting of a small stock of groceries and book ac-

counts, for the sole purpose of preventing a levy upon same by attachment, his trustee in bankruptcy is entitled to have the bill of sale set aside as fraudulent as against the creditors. *Thomas v. Fletcher*, 18 A. B. R. 624, 153 Fed. 226 (D. C. Me.).

26. Only testimony that of parties themselves, which show valid transfer. *Entwisle v. Seidt*, 19 A. B. R. 185, 155 Fed. 864 (D. C. N. Y.).

27. Transfer merely preferential and not fraudulent, not voidable in New Jersey. *Manning v. Evans*, 19 A. B. R. 217, 156 Fed. 106 (D. C. N. J.).

Transfer where transferor was a man reputed of great wealth, etc. *Coder v. Arts*, 22 A. B. R. 1, 213 U. S. 223.

28. Transfer not fraudulent but merely to get money to make preferential payments. (*Van Iderstine*) *Trustee v. Natl. Discount Co.*, 23 A. B. R. 345, 174 Fed. 518 (C. C. A. N. Y.).

29. Deed of trust. In *re Elletson Co.*, 23 A. B. R. 530, 174 Fed. 859 (D. C. W. Va.).

Transfer by bankrupt to wife of real estate and of mortgage acquired through real estate speculations carried on on wife's money held in trust by bankrupt, held a valid recognition of "trust." *Butcher v. Cantor*, 26 A. B. R. 424, 185 Fed. 945 (D. C. N. Y.).

the act, that the filing of the petition is something more than the dedication by the bankrupt of his property to the payment of his debts; that the trustee is not only invested with the title of the property, but since, after the filing of the petition, the creditors are powerless to pursue and enforce their rights, the trustee is vested with their rights of action with respect to all property of the bankrupt transferred by him or encumbered by him in fraud of his creditors, and may assail, in behalf of the creditors, all such transfers and encumbrances to the same extent that creditors could have done had no petition been filed. The filing of the petition, followed by seizure and by adjudication in bankruptcy, is a seizure of the property by the law for the benefit of creditors, and an appropriation of it to the payment of the debts of the bankrupt. It is a seizure of the property by legal process, equal in rank to and of the same force and effect as by execution or attachment." [The last sentence whilst a true statement since the Amendment of 1910 was not accurate before that Amendment, when this case was decided.]

In *re Rudnick*, 4 A. B. R. 534, 102 Fed. 750 (D. C. Wash.): "The right and title of a trustee is, in general, the same as the right and title which the bankrupt possessed prior to the adjudication, but to this is added authority to avoid fraudulent transfers of property." [The trustee has more than "the same right and title which the bankrupt possessed prior to the adjudication," now, by the Amendment of 1910.]

In *re Shaw*, 17 A. B. R. 206 (D. C. Me.): "In the case at bar the testimony tends to show that, at the time of giving of the mortgage to the bank, Shaw was insolvent, that there was an obvious attempt to make the delivery to the mortgagee secret, rather than open, and that there was a distinct and affirmative understanding that the mortgage was not to be recorded. The case discloses a want of good faith, resulting in an actual fraud upon the general creditors."

Norcross v. Nathan, 3 A. B. R. 622 (D. C. Nev.): "The trustee in bankruptcy stands in the place of the creditors of the bankrupt, and has the same rights and may pursue the same remedies in their behalf as they could or would have been entitled to if there had been no adjudication in bankruptcy." [This statement was made in connection with property fraudulently transferred.]

In *re Gray*, 3 A. B. R. 647 (N. Y. Sup. Ct. App. Div.): "When, however, the trustee seeks to avoid a fraudulent or any avoidable transfer by the bankrupt antedating the four months, he does so, not in the right conferred as a concomitant to the due operation of the system, but exclusively in the creditors' common-law right. He is, with relation to these anterior transfers, so to speak, subrogated to that right. Such of these anterior transfers as any creditor might have avoided, he may avoid. Such as no creditor could have avoided, he cannot avoid."

A sale, although for present valuable consideration, may be set aside if made with fraudulent intent participated in by the purchaser.⁷¹

⁷¹ *Johnston v. Forsyth Mercantile Co.*, 11 A. B. R. 669, 127 Fed. 845, 19 A. B. R. 43 (D. C. Ga.); instance, *Houck v. Christy*, 18 A. B. R. 330, 152 Fed. 612 (C. C. A. Kans.); *obiter*, *Thomas v. Fletcher*, 18 A. B. R. 624, 153 Fed. 226 (D. C. Me.). Likewise as to a mortgage for a valid debt, *In re Elletson Co.*, 23 A. B. R. 530, 174 Fed. 859 (D. C. W. Va.); *Johnston v. Forsyth Mercantile Co.*, 11 A. B.

R. 669, 127 Fed. 845 (D. C. Ga.); *obiter*, *McNulty v. Wiesen*, 12 A. B. R. 342, 130 Fed. 1012 (D. C. Penn.).

Obiter (principle conceded), *Gorham v. Buzzell*, 24 A. B. R. 440, 178 Fed. 596 (D. C. Me.).

Compare, as to setting aside the purchase of an annuity, as being in fraud of creditors, though for a present valuable consideration, post, §§ 1018½. Compare also §§ 1495, 1496.

Obiter, Coder v. Arts, 22 A. B. R. 1, 213 U. S. 233: “* * * and it makes no difference that the conveyance was made upon a valuable consideration, if made for the purpose of hindering, delaying or defrauding creditors. The question of fraud depends upon the motive.”

Obiter, In re Pease, 12 A. B. R. 68, 129 Fed. 446 (D. C. Mich.): “Even though a present, fair consideration be paid for property transferred to the hindrance, delay of, or in fraud upon creditors, it will not save the conveyance. ‘A sale may be void for bad faith, though the buyer pays the full value of the property bought.’ This is the consequence where his purpose is to aid the seller in perpetrating a fraud upon his creditors, and where he buys recklessly, with guilty knowledge.”

Thomas v. Fletcher, 18 A. B. R. 623, 153 Fed. 226 (D. C. Me.): “I have had occasion before, when issues of this sort have been presented, to refer to *Blennerhassett v. Sherman*, 105 U. S. 100, in which the court said: ‘It is not enough, in order to support a settlement against creditors, that it be made for a valuable consideration. It must also be bona fide. If it be made with intent to hinder, delay, or defraud them, it is void as against them, although there may be in the strictest sense a valuable or even an adequate consideration.’ In *Davis v. Schwartz*, 155 U. S. 631, Mr. Justice Brown, in speaking for the Supreme court, said: ‘It has been the accepted law ever since *Twyne’s Case*, 3 Coke, 80, that good faith, as well as a valuable consideration, is necessary to support a conveyance as against creditors. In that case *Pierce*, being indebted to *Twyne* in £400, was sued by a third party for £200. Pending such suit, he conveyed all his property to *Twyne* in consideration of his debt, but continued in possession, sold certain sheep, and set his mark on others. It was resolved to be a fraudulent gift, though the deed declared that it was made bona fide. Most of the cases illustrative of this doctrine, however, have been like that of *Twyne*, wherein a debtor, knowing that an execution was to be taken out against him, had sold his property to a vendee having knowledge of the facts, for the express purpose of avoiding a levy, or receiving a consideration which could not be reached by execution. In such cases the fact that he receives a good consideration will not validate the transaction, unless at least the creditor has obtained the benefit of the consideration.’”

Thus, the sale, hurriedly, by a retail merchant, of his entire stock of goods, throws the burden upon the purchaser of inquiring into the seller’s financial condition.⁷²

Allen v. McMannes, 19 A. B. R. 276, 156 Fed. 615 (D. C. Wis.): “The sale of an entire stock of goods of a retail merchant is a suspicious circumstance per se, naturally calculated to put the purchaser on inquiry. *Walbrun v. Babbitt*, 16 Wall. 577, 21 L. Ed. 489; *In re Knopf* (D. C.), 16 Am. B. R. 432, 146 Fed. 109; *Dokken v. Page*, 17 Am. B. R. 228, 147 Fed. 438, 77 C. C. A. 674. Such a purchase is presumptively questionable, and casts the burden of proof on the purchaser to show that he had no notice of facts or circumstances sufficient to arrest his attention, puts him on inquiry, and requires him to use such means of knowledge as were at hand in order to learn whether the seller is not in financial difficulty, and whether a general statement, such as that the book accounts are sufficient to pay the mercantile creditors, was true.”

⁷² *In re Knopf*, 17 A. B. R. 48 (D. C. S. Car.); impliedly, *Houck v. Christy*, 18 A. B. R. 330, 152 Fed. 612 (C. C. A. Kans.). Compare, inferen-

tially, *In re Calvi*, 26 A. B. R. 206, 185 Fed. 642 (D. C. N. Y.). Compare further instances in note 70.

But the mere selling out of the usual course of business is not of itself proof, nor does it make a *prima facie* case of fraudulent intent, alone considered.^{72a}

And tender of the actual consideration received for the transfer is not necessary when the suit is in behalf of creditors.⁷³ Nor is it necessary to trace the actual consideration paid upon setting aside the purchase of an annuity not yet matured.⁷⁴

Pretended "warehousings" and the pledging of warehouse receipts based thereon, and similar transactions, the debtor retaining possession and power of disposition, are fraudulent and void as against the trustee.⁷⁵

Chattel mortgages with powers of sale, are void as against the trustee where there is no agreement that the proceeds be applied on the debt, where such mortgages are held void as to creditors by the law of the State.⁷⁶

Conditional sales of personal property, where the conditional buyer has the power of selling in the usual course of business, are, in general, void.⁷⁷

Property that never stood in the bankrupt's name may nevertheless be recovered, if title was taken and is held by another on secret trust for him.⁷⁸

Likewise, where goods are nominally sold to a go-between corporation whose stock, all but two shares, is owned by the bankrupt and which was organized for the very purpose of protecting the seller in its dealings with the bankrupt, it has been held that the nominal buyer was the "alter ego" of the bankrupt and that the goods in its possession belonged to the bankrupt estate.⁷⁹

There must exist an intent to hinder, delay or defraud, more than merely the making of the transfer itself necessarily would cause, to render the transfer fraudulent, where the transfer is applied upon a pre-existing debt.⁸⁰

Coder v. Arts, 18 A. B. R. 513, 152 Fed. 943 (C. C. A. Iowa): "A transfer by an insolvent, within four months prior to the filing of a petition, for the purpose of securing or paying a pre-existing debt, without any intent or purpose to affect other creditors injuriously beyond the necessary effect of the security, is lawful, if not violative of other provisions of law, and it does not evidence any intent to hinder, delay or defraud creditors within the meaning of Bankruptcy Act, 1898, § 67e."

The intent need not be actually to cheat and defraud; it is enough if it

72a. *Houck v. Christy*, 18 A. B. R. 330, 152 Fed. 612 (C. C. A. Kans.).

73. *Johnston v. Forsyth Mercantile Co.*, 11 A. B. R. 669, 127 Fed. 845 (D. C. Ga.).

74. *Smith v. Mutual Life Ins. Co.*, 24 A. B. R. 514, 178 Fed. 510 (C. C. Mass.).

75. (*Security*) *Warehousing Co. v. Hand*, 19 A. B. R. 291, 206 U. S. 415; *In re Gebbie*, 21 A. B. R. 694, 167 Fed. 609 (D. C. Pa.). Also, see §§ 1146 and 1228.

76. See § 1257 et seq.

77. See post, § 1263. See also, *Gilligan (Troy Wagon Works v. Hancock)*, 23 A. B. R. 668, 152 Fed. 605 (C. C. A. Ind.).

78. See next section, § 1210.

79. *Ludvig v. Woolen Co.*, 19 A. B. R. 795, 159 Fed. 796 (D. C. N. Y.).

80. *Sargeant v. Blake*, 20 A. B. R. 115, 160 Fed. 57 (C. C. A. Mo.), quoted post, § 1498; *Allen v. Gray*, 21 A. B. R. 828 (N. Y. Sup. Ct.).

be to hinder and delay; and it does not alter the legal effect that the debtor honestly believed that by making such conveyance he would be able to continue in business and in time work out of it a profit sufficient to pay all debts; nor that the transferee shared in such belief.

In *re Elletson Co.*, 23 A. B. R. 530, 174 Fed. 859 (D. C. Va.): "The intent may not be to actually cheat and defraud; it is enough if it be to hinder and delay. A debtor may honestly believe that by making such conveyance of personal property he will be able to continue in business and in time work out of it a profit sufficient to pay all debts existing and that may be incurred in accomplishing this purpose. The favored creditor, to be secured may share in this view and be willing to sell his property on long time thus secured, in order to allow the experiment to be tried. But it is not sound morality nor good law to allow these two to determine the rights of others, or to hinder or delay those others in the enforcement of their rights."

And intent may be gathered from surrounding circumstances.⁸³

But the transfer of exempt property cannot be set aside as fraudulent.⁸⁴

The discharge of the bankrupt does not affect the right of recovery.^{84a}

The trustee may sell his interest in property, which has been fraudulently transferred without having recovered the property.

In *re Downing*, 27 A. B. R. 228, 201 Fed. 93 (C. C. A. N. Y.): "The trustee has a transferable interest in real estate owned by the bankrupt and transferred by him in fraud of his creditors, even though made more than four months prior to the proceedings in bankruptcy and may sell this interest, together with the right vested in him by statute to maintain an action to set aside such fraudulent transfer. The sale is to be made without warranty or representation of any kind and the purchaser takes simply the trustee's interest in the real property and his right to bring an action. The right may be valuable and it may be worthless; whoever buys does so with a full understanding of the character of the claim, he cannot be misled into thinking that the District Court or this court has in any way recognized the validity of the claim by directing that it be sold."

§ 1210. Likewise, Property Not "Transferred" by Bankrupt but Held on Secret Trust for Him.—Likewise property not "transferred" by the bankrupt, but obtained in the name of another for his benefit or otherwise fraudulently held in trust for him, is recoverable by the trustee.⁸⁵

Before the Amendment of 1910 to Bankr. Act, § 47 (a) (2), giving the trustee the rights, remedies and powers of a creditor under state law armed with process, it was doubted, in some decisions, whether under Bankr. Act, § 70 (a) (4) and (e) the trustee could take property held under

⁸³. In *re Ellertson Co.*, 23 A. B. R. 530, 174 Fed. 859 (D. C. Va.).

⁸⁴. *Cowan v. Burchfield*, 25 A. B. R. 293, 180 Fed. 614 (D. C. Ala.).

^{84a}. *Evans v. Staalle*, 11 A. B. R. 182, 92 N. W. (Minn.) 951.

⁸⁵. Instance where property held in the name of another on secret trust or resulting trust in favor of the bank-

rupt: *Evans v. Staalle*, 11 A. B. R. 182, 92 N. W. 951 (Minn.). Although in this case the court said the property did not belong to the trustee. Also, see *Fowler v. Jenks*, 11 A. B. R. 255, 90 Minn. 74; *Merrill v. Hussey*, 16 A. B. R. 816, 64 Atl. (Me.) 819, in which case title was fraudulently taken in the name of another.

fraudulent trust for the bankrupt but which had never been in the bankrupt's name and hence never had been "transferred" by him, the Bankr. Act, §§ 70 (a) (4) and (e), and 67 (e), under which he derived his rights as against fraudulent transactions referring only to fraudulent "transfers" by the bankrupt, such decisions, however, conceding that he might do so under Bankr. Act, § 67 (a) and (f), if a creditor armed with process existed, to whose right he might be subrogated.

Analogously, *London v. Epstein*, 24 A. B. R. 557, 123 App. Div. N. Y. 399: "In fine, the difficulty in the way of the plaintiff is that the fee never was in the bankrupt, but always in third parties; that neither legal nor equitable interest in this property ever existed in the bankrupt; that he 'had no remaining right on which, through judgment and execution, creditors could by any process fasten a specific lien.' The statute that declares the resulting trust is solely for the benefit of certain creditors and makes against 'the property of a third party which the debtor never owned.'"

But such was doubtless a too narrow construction of the extent of the Bankruptcy Act's provisions relative to fraudulent transactions even before the Amendment of 1910 unless the State law required the existence of a levying creditor in such instances; for property held on secret trust for the bankrupt was recoverable by the trustee as being the bankrupt's property, the fraudulent holding in another's name not making it any the less his property.

However, the question is practically set at rest by the Amendment of 1910, to § 47 (a) (2), for by that Amendment the trustee is endowed with all the rights of a creditor under state law, among which would be found always the right to subject property held on fraudulent trust for the bankrupt though never standing in the bankrupt's name.

§ 1211. Constructively Fraudulent Though Not Actually So.—That the transaction is merely "fraudulent in law," without intentional bad faith, does not alter the rule.⁸⁶

In re Standard Tel. & Elec. Co. (*Knapp v. Milw. Tr. Co.*) 24 A. B. R. 761, 216 U. S. 545 (aff'g *Knapp v. Milw. Tr. Co.*, 20 A. B. R. 671, 162 Fed. 675): "While there was a finding that no intentional bad faith was shown, still we agree with the Court of Appeals and the district judge that, under the law of Wisconsin, as construed by her highest court, such conditions as were contained in these mortgages rendered them fraudulent in law and void as to creditors. * * * In this case the stipulations of the mortgages practically permitted the mortgagor to dispose of the property for his own benefit except that it must make certain provisions for a sinking fund and interest on the bonds; and, with the consent of the trustee, no provision need be made for the sinking fund, or interest, and the moneys which otherwise would have been placed therein for the purchase of bonds might be applied for the benefit of the mortgagor, whether as dividends or for the benefit of its business and

86. See same doctrine, § 1257, et seq.

property. Such provisions are clearly within the Wisconsin decisions, for they permit the mortgagor to have the benefit of the property, to keep it in his possession, and to appropriate the proceeds to his own use. The Wisconsin decisions render such mortgages invalid as to creditors, because the effect of such provisions is to give the beneficial use of the mortgaged property to the mortgagor in possession, and to make possible the use of the mortgage as a protection against creditors of the mortgagor when they shall undertake to assert their rights.

"But it is said the trustee in bankruptcy may not defend against these mortgages. It is contended that they are good as between the parties, and that as to them the trustee in bankruptcy occupies no better position than the bankrupt."

"The principles announced in *Security Warehousing Co. v. Hand*, 206 U. S. 415, 19 Am. B. R. 291, when applied to the present case are decisive of the question here presented. Under the Wisconsin statutes and decisions of the highest court of that State the conditions contained upon the face of this mortgage were such as to render it fraudulent in law and void as to creditors, and prior to the filing of the petition in bankruptcy the property might have been levied upon and sold by judicial process against the bankrupt.

"It is true that in *Security Warehousing Co. v. Hand* the court said that the attempted pledge was a 'mere pretense, a sham;' but the courts of Wisconsin have held that such provisions as are in these mortgages, giving the bankrupt the right to dispose of the mortgaged property for its own benefit, rendered the conveyance fraudulent in law, and therefore void as to creditors. This brings the conveyance within the terms of the Bankruptcy Act, as one which the trustee may attack, as conclusively as it would if fraudulent intent in fact were shown to exist." Quotations from this decision are further found at § 1258; and, on questions of procedure, at § 2875 and § 2969.

§ 1211½. Fraudulent or Preferential Transfers by State Law Inuring to Benefit of All Creditors, Whether So Inure in Bankruptcy.

—Fraudulent or preferential transfers declared by State law, as matter of substantive law and not merely as remedial law, to inure to the benefit of all creditors, will operate to the benefit of all creditors in Bankruptcy.⁸⁷

Impliedly, *Pollock v. Jones*, 10 A. B. R. 616, 124 Fed. 163 (C. C. A. S. C., affirming 9 A. B. R. 262): "In South Carolina it is declared that assignments by an insolvent debtor giving priority or preference, are null and void. Code Civ. Proc., § 2647. Construing this act, the Supreme Court of the State has held that an instrument, although in form of a mortgage, if it disposes of the whole of the grantor's estate for the purpose of securing a creditor, is in fact an assignment for creditors, to be construed and controlled as such. * * *

"We are of the opinion that, both under the statute law of South Carolina and the provisions of the Bankrupt Law, A. H. Pollock cannot claim under this mortgage against the estate of the Bankrupt."

Morgan v. Nat'l Bk., 16 A. B. R. 644, 145 Fed. 466 (C. C. A. W. Va.). "The

⁸⁷. *Union Trust Co. v. Amery*, 27 A. B. R. 499 (Sup. Ct. Wash.); impliedly, see suggestion in dissenting opinion of Day, J., in *Keppel v. Tiffin Sav. Bk.*, 13 A. B. R. 552, 197 U. S. 356; instance, *Wright v. Gansevoort Bk.*, 17 A. B. R. 326 (N. Y. Sup. Ct.):

Preferential transfer in contemplation of insolvency under New York State Stock Corporation Law.

Compare, however, *Moore v. Green*, 16 A. B. R. 648, 145 Fed. 480 (C. C. A. W. Va.).

trust deed, moreover, was void under the statute of West Virginia to the extent that it sought to prefer one creditor over another, provided the same was assailed within four months of the recordation thereof, and by reference to § 67 (e) of the Bankruptcy Act such invalidity is expressly recognized."

In *re Kohler*, 20 A. B. R. 89, 159 Fed. 871 (C. C. A. Ohio): "Sections 6343 and 6344 of the Revised Statutes of Ohio regulate the recovery and distribution of property conveyed in fraud of creditors. Section 6343 provides that every sale or transfer procured by a debtor to be rendered with intent to hinder, delay or defraud creditors, shall be declared void as to creditors of such debtor at the suit of any creditor or creditors 'as hereinafter provided,' and shall operate as an assignment and transfer of all the property and effects of such debtor, and shall inure to the equal benefit of such creditor or creditors in proportion to the amount of their respective demands, including those which are unmatured. Section 6344 provides that any creditor, as to whom any of the acts prohibited in § 6343 are void, 'whether the claim of such creditor has matured or will thereafter mature,' may commence an action to have such act declared void, and such court shall appoint a trustee, who shall proceed by due course of law to recover possession of all property so sold, etc., 'and to administer the same for the equal benefit of all creditors,' as in other cases of assignment to trustees for the benefit of creditors. These sections appear to us to provide clearly that where property is conveyed in fraud of creditors, it may be recovered by a trustee 'for the equal benefit of all creditors,' and we understand this to mean for the equal benefit of all creditors, not part of them, not simply those existing at the time the transfer was fraudulently made."

Clingman v. Miller, 20 A. B. R. 360, 160 Fed. 326 (C. C. A. Kans.): "The law of Kansas does not prohibit preferences, but it does say that if a debtor makes a deed of general assignment for the benefit of his creditors he must treat all alike, and that he cannot evade this prohibition of the statute by making simultaneously with the deed of assignment a separate transfer which creates a preference. The preference would be void if contained in the deed of assignment, and it is no less so because made outside of it, but at the same time and as a part of the same transaction. The intent of Pendleton is the true and guiding principle. As was said in *Lumber Co. v. Ott*, supra, at page 630: 'With what intent did Ott in this case execute the various instruments prior to the general assignment? Was he intending a general assignment, and seeking to evade the statute, and to give preferences by other instruments? Or was he, finding himself involved and likely to be closed out by some of his creditors, simply preferring some, uncertain as to what disposition he should make of the balance of his property after they had been secured?' The knowledge, or want of knowledge, of the purpose and intent of Pendleton at the time of the transfer by Miller & Co. is immaterial under the laws of Kansas; otherwise, the prohibition of the statute would be rendered useless."

Thus, preferential transfers under the New York Stock Corporation Law have repeatedly been held available to creditors in bankruptcy.⁸⁸

Again, where State law declares to be preferential a transfer which is

88. *Wright v. Gansevoort Bank*, 18 A. B. R. 363, 118 App. Div. 281; *Perry v. Van Norden Trust Co.*, 20 A. B. R. 190 (N. Y. Ct. App.), where bona fide purchaser for value protected; *Wright v. Skinner Mfg. Co.*, 20 A. B. R. 527,

162 Fed. 315 (C. C. A. N. Y.); *Wright v. Gansevoort Bank*, 17 A. B. R. 326; inferentially, *In re Salvator Brewing Co.*, 25 A. B. R. 536, 183 Fed. 910 (D. C. N. Y.).

not preferential under the Bankrupt Act, the trustee in bankruptcy may succeed to the rights of any creditor who has already instituted proceedings under the State law, and the lien of such proceedings may be preserved; for example, where by State law the transfer of individual property by one member of a partnership, not himself adjudged bankrupt, is held to be preferential as to the firm creditors.⁸⁹ So, also, as to voidable sales under the New Jersey "Act to prohibit sales of merchandise in bulk in fraud of creditors."⁹⁰

In such instances it seems that the four months limitation does not apply.⁹¹

But it is well settled that the United States alone can complain of a violation of § 5201, Rev. Stat., which, in some instances, prohibits a national bank from accepting a pledge of its own capital stock.⁹² Nor does this statute prohibit a national bank from accepting its capital stock as security, where such action is necessary for the protection of a pre-existing debt to secure the bank against loss.⁹³

§ 1212. "Creditor Armed with Process" Not Requisite.—In suits by the trustee to recover property fraudulently transferred, it is not requisite that there exist a creditor "armed with process," the Bankruptcy Act itself, in § 70 (a) (4), specifically providing that title to such property shall pass to the trustee.^{93a}

Thomas v. Roddy, 19 A. B. R. 873, 122 App. Div. 857, 107 N. Y. Supp. 473: "The trustee, by this provision of the act, is invested with the title of all property of the bankrupt transferred by him in fraud of creditors, unless his right in this respect is restricted—which I do not believe it is—by subdivision e. The policy of the act is to secure an equal distribution of all property of the bankrupt among all his creditors. For that purpose the trustee represents all the creditors and may maintain an action to set aside any transfer which any creditor could or which any creditor might acquire by any process taken by him. *Matter of McNamara*, 2 Am. B. R. 566; *Mueller v. Bruss*, 8 id. 442; *Sheldon v. Parker*, 11 id. 152; *Beasley v. Coggins*, 12 id. 355. Under the Bankruptcy Act of 1867, which contained a provision to the effect that title to property fraudulently transferred vested in the assignee, now the trustee, it was held that the assignee could maintain an action to set aside such transfers whether

89. *Miller v. Acid & Fertilizer Co.*, 21 A. B. R. 416, 211 U. S. 496 (quoted at §§ 1441, 1489, 1491).

90. *In re Lipman*, 29 A. B. R. 139, 201 Fed. 169 (D. C. N. J.). As to trustee's rights under Ante Bulk Sales Laws, in general, see post, § 1269½.

91. Inferentially, *In re Salvator Brewing Co.*, 25 A. B. R. 536, 183 Fed. 910 (D. C. N. Y.). Compare, post, § 1214.

92. *First Nat. Bank v. Lanz*, 29 A. B. R. 247, 202 Fed. 117 (C. C. A. La.).

93. *First Nat. Bank v. Lanz*, 29 A. B. R. 247, 202 Fed. 117 (C. C. A. La.).

93a. For this same proposition,

see ante, § 1209. See also, *Warehousing Co. v. Hand*, 19 A. B. R. 291, 206 U. S. 415, quoted at § 1209; *In re Gebbie & Co.*, 21 A. B. R. 691, 167 Fed. 609 (D. C. Pa.), quoted at § 1209; *Fourth St. Nat. Bank v. Millbourne Mills Co.*, 22 A. B. R. 442, 172 Fed. 177 (C. C. A. Pa.), quoted at § 1146; *In re Bellevue Pipe & Foundry Co.*, 22 A. B. R. 99, 16 Ohio Decisions 247 (Ref. Ohio); *In re Penny & Anderson*, 23 A. B. R. 105 (Ref. N. Y.); *In re Standard Tel. & Elect. Co.* (*Knapp v. Milw. Tr. Co.*), 216 U. S. 545, 24 A. B. R. 761, quoted at §§ 1211, 1258.

any individual creditor could have done so or not. *Platt v. Matthews*, 10 Fed. 280; *Matter of Leland*, 10 Blatchf. 503. Judge Wallace, who delivered the opinion in the *Matthews* case, concluded by saying: 'Numerous other authorities might be cited to sustain the position that an assignee may proceed to recover property transferred in fraud of creditors whether any creditor was in a position to attack the transfer or not, and that his title accrues by force of the act, and not through the rights of the creditor to assert the fraud.' The same view was entertained by the Court of Appeals in *Southard v. Benner*, 72 N. Y. 424. There the court had under consideration the construction to be put upon chapter 314 of the Laws of 1858 in connection with the Bankruptcy Act of 1867. The provisions of that act are somewhat similar to the one under consideration in so far as relates to the maintenance of an action by an assignee or a trustee, irrespective of the rights of individual creditors. The court, speaking through Judge Allen, said: 'Upon sound reason and the policy of the law, as well as the authorities quoted and others that might be referred to, there can be no doubt, we think, that the plaintiff as assignee has a right of action for property conveyed by the bankrupt in fraud of his creditors, although none of the creditors have acquired a specific lien. It is not such liens, or any particular interest in the property, or an interest for the benefit of any one creditor or class of creditors, that is vested in the assignee, but the entire property fraudulently transferred and for the benefit of all the creditors. The assignee takes title not under any claim of right existing in the creditors, but under the statute, and that right he may assert by action, although no individual creditor, or all the creditors combined, could have a standing in court to challenge the conveyance.' Therefore, it seems to me, even though it be held, as contended, that the complaint does not show that any of the creditors whose claims were filed in the bankruptcy proceeding were in a position to attack the transfers, nevertheless, the trustee may do so. This must be so if the reasoning in the authorities cited be sound. To hold that a trustee cannot attack a fraudulent conveyance made by the bankrupt more than four months before the filing of the petition, without showing that some creditor had obtained a judgment and issued execution thereon, so that he could maintain a similar action, would be simply to provide an easy and convenient method for a dishonest debtor to dispose of his property. In that case the debtor could fraudulently dispose of all his property more than four months before bankruptcy proceedings were instituted, and unless some creditor—intermediate the disposition of the property and the filing of the petition in bankruptcy—had put himself in position to attack the fraudulent transfers by obtaining a judgment, issuing an execution and having the same returned unsatisfied, the trustee would be powerless to reach the property fraudulently disposed of."

Thus, the trustee may bring an action for trespass on the case based on a conspiracy to fraudulently secrete and transfer the bankrupt's property.⁹⁴ Likewise he may proceed to set aside chattel mortgages with power of sale.⁹⁵

But property fraudulently bought and held in the name of another, title never having been in the bankrupt, was held before the Amendment of 1910, not recoverable by the trustee under the New York statutes, since the trustee was not in the position of a judgment creditor whose remedies

94. *Sattler v. Slonimsky*, 28 A. B. R. 729, 199 Fed. 592 (D. C. Pa.).

95. *In re Hartman*, 26 A. B. R. 76, 185 Fed. 196 (D. C. N. Y.).

at law had been exhausted;⁹⁶ but the Amendment of 1910 [Bankr. Act, § 47] has given such rights now to the trustee.^{96a}

§ 1213. Badges of Fraud Considered Together, Not Separately.—Badges of fraud are to be considered together, not separately.⁹⁷

Houck v. Christy, 18 A. B. R. 330, 152 Fed. 612 (C. C. A. Kans.): "Moreover, we think the evidence before recited brings the case well within the rule that badges of fraud, altogether inconclusive if separately considered, may, by their number and joint operation, especially when corroborated by moral coincidences, be sufficient to constitute conclusive proof of fraudulent intent on the part of both vendor and vendee."

Orr v. Park, 25 A. B. R. 544, 183 Fed. 683 (C. C. A. Ga.): "Dunn Bros. remaining in possession of the goods, continuing business, and selling goods, just as before the mortgage was made; their failure to sign the mortgage and have it witnessed until from one to three months after it purports to have been made; their possession of the mortgage subsequent to their signing it; and the withholding it from record—are badges of fraud which were sufficient, in our opinion, to warrant the judgment and finding of the referee that the mortgage was made to hinder, delay, and defraud the creditors of said Dunn Bros., and was null and void, in which judgment and finding we concur."

§ 1213½. Great Latitude in Admission of Evidence.—Questions of fraud can scarcely ever be proved by direct evidence, and great latitude is to be allowed in the admission of all the circumstances fairly connected with the case.⁹⁸

§ 1213¾. Conspiracy to Defraud.—Action may be brought by the trustee against several defendants for conspiracy to defraud creditors,⁹⁹ although it is held in one case that it must appear that property was actually taken.¹ However, the latter holding seems to lose sight of § 70 (a) (6), which passes title to the trustee to "rights of action arising * * * from the unlawful taking or detention of, or injury to" the bankrupt's property.

At any rate, such action may not be brought in the District Court if it be a suit merely for damages for the conspiracy and not a suit to recover property, or the value of property wrongfully transferred by the bankrupt.²

96. *London v. Epstein*, 24 A. B. R. 557 (N. Y. App. Div.), quoted at § 1210; *In re Downing*, 27 A. B. R. 309, 192 Fed. 683 (D. C. N. Y.).

Trustee Selling Right of Action to Set Aside Fraudulent Conveyance.—Whether purchaser of real estate from trustee may maintain suit in trustee's name to set aside fraudulent transfer, see ante, § 1209.

96a. See ante, § 1209, and post, § 1270 1-10, et seq.

97. See also, post, §§ 1496½, 1504; ante, § 109.

98. *In re Lubber*, 18 A. B. R. 476, 152

Fed. 492 (D. C. Pa.); also, see ante, §§ 114½, 856¾.

99. See ante, § 358½, post, §§ 1742½, 2328½; also, see *Strasburger v. Bach*, 19 A. B. R. 732, 157 Fed. 918 (C. C. A. Ills.); instance, apparently, *Ludwig v. Am. Woolen Co.*, 19 A. B. R. 795, 159 Fed. 796 (D. C. N. Y.); contra, where no goods received by conspirators, *Friedman v. Myers*, 19 A. B. R. 883, 30 Ohio C. C. Rep. 303.

1. *Friedman v. Myers*, 19 A. B. R. 883, 30 Ohio C. C. 303.

2. Compare, post, §§ 1692, 1694; also see *Lynch v. Bronson*, 24 A. B. R. 513, 177 Fed. 605 (D. C. Conn.), quoted at § 1694.

§ 1214. Fraudulent Transfers before Four Months of Bankruptcy.—Even fraudulent transfers made previously to the four months period may be set aside at the suit of the trustee and the assets held for creditors.³

Beasley v. Coggins, 12 A. B. R. 355, 48 Fla. 215 (Sup. Ct. Fla.): "Under the Bankruptcy Act, when one is thereunder adjudged a bankrupt, creditors are not permitted to attack fraudulent conveyances of their debtor, made more than four months of the adjudication of bankruptcy; and, if the trustee could not do so, then the act would constitute 'a device to permit fraudulent conveyances to take effect with impunity in case they are successfully concealed for the specified four months.'"

Obiter, *Babbitt v. Kelley*, 9 A. B. R. 338 (St. Louis Ct. App.): "A trustee in bankruptcy may sue to set aside a conveyance made by a bankrupt in actual fraud of creditors earlier than four months prior to the instituting of the proceedings in bankruptcy, and in fact is only barred by the limitation period which would bar creditors whom he represents."

Thus as to "voluntary conveyances" by way of gift, to hinder and delay creditors,⁴ or transfers for nominal considerations, for the same purpose, as, for example, to avoid levy of attachment.⁵

So, also, it seems that the trustee may sell his interest in property so transferred, together with the right to bring action for its recovery.⁶

§ 1215. Fraudulent Transfers before Passage of Bankruptcy Act.—Also fraudulent transfers made before the passage of the Bankruptcy Act itself may be set aside.⁷

3. *Hull v. Hudson*, 26 A. B. R. 725 (Ch. Ct. Del.); *Kirkpatrick v. Johnson*, 28 A. B. R. 291, 197 Fed. 235 (D. C. Pa.); *Peterson v. Mettler*, 29 A. B. R. 158, 198 Fed. 938 (D. C. Wash.); *Hobbs v. Frazier*, 26 A. B. R. 887 (Sup. Ct. Fla.); instance, *Cowan v. Burchfield*, 25 A. B. R. 293, 180 Fed. 614 (D. C. Ala.); *Jackson v. Sedgwick*, 26 A. B. R. 836, 189 Fed. 508 (C. C. N. Y.); *Bush v. Export Storage Co.*, 14 A. B. R. 141, 136 Fed. 918 (C. C. Tenn.); obiter, *In re Schenck*, 8 A. B. R. 727, 116 Fed. 555 (D. C. Wash.); *Skillen v. Endelman*, 11 A. B. R. 766, 79 N. Y. Supp. 413, 39 Misc. 261; *Pratt v. Christie*, 12 A. B. R. 1 (N. Y. Sup. Ct. App. Div.); *In re Adams*, 1 A. B. R. 94 (Ref. N. Y.); *In re Grohs*, 1 A. B. R. 465 (Ref. Ohio); *In the bankruptcy court itself: In re Scrinopskie*, 10 A. B. R. 221 (D. C. Kas.); *In re Chaplin*, 8 A. B. R. 121 (D. C. Mass.); contra (not in the bankruptcy court), *In re Grohs*, 1 A. B. R. 465 (Ref. Ohio); *In the State Court: Mueller v. Bruss*, 8 A. B. R. 442, 112 Wis. 406; *Andrew v. Mather*, 9 A. B. R. 299, 134 Ala. 358;

Thomas v. Roddy, 19 A. B. R. 873, 122 App. Div. 851, 107 N. Y. Supp. 473, quoted, on other points at § 1212. *Phillips Tr. v. Kleinman*, 23 A. B. R. 266 (Pa. Com. Pleas); *In re Elletson Co.*, 23 A. B. R. 530, 174 Fed. 859 (D. C. W. Va.), quoted post, at § 1888. Similarly, under the law of 1867, *Hyde v. Sontag*, 8 N. B. Reg. 225.

Compare, inferentially, *In re Solvator Brewing Co.*, 25 A. B. R. 536, 183 Fed. 910 (D. C. N. Y.).

4. *In re Schenck*, 8 A. B. R. 727, 116 Fed. 555 (D. C. Wash.); obiter, *In re Toothacker Bros.*, 12 A. B. R. 99, 128 Fed. 187 (D. C. Conn.).

5. *Thomas v. Fletcher*, 18 A. B. R. 623, 153 Fed. 226 (D. C. Me.).

6. Compare ante, § 1209; also see *In re Downing*, 27 A. B. R. 309, 192 Fed. 683 (D. C. N. Y.).

7. *In re Adams*, 1 A. B. R. 94 (Ref. N. Y.); inferentially, *In re Gaylord*, 7 A. B. R. 1, 112 Fed. 668 (C. C. A. N. Y.); *In re Brown*, 1 A. B. R. 107, 91 Fed. 358 (D. C. Ore.); (1867) *Cady v. Whaling*, Fed. Cases No. 2,285, 7 Biss. 430.

§ 1215¹. **Insolvency, Whether Requisite.**—There are several different sections of the Bankruptcy Act giving rights to the trustee as to property fraudulently transferred. Thus, § 70 (a) (4) vests *title* in the trustee to all "property transferred by him [the bankrupt] in fraud of his creditors." Again, § 70 (e) provides that "the trustee may avoid any transfer by the bankrupt of his property which any creditor of such bankrupt might have avoided." Section 67 (e) also has two clauses somewhat differing in their provisions as to fraudulent transfers, but both limited to transfers occurring within four months preceding the bankruptcy. The first of these clauses [discussed post at § 1493, et seq.] does not require, in *hæc verbis*, proof of insolvency in order to establish a *prima facie* case, but the second clause does require such proof, in the following words:

"And all conveyances, transfers or incumbrances of his property made by a debtor at any time within four months prior to the filing of the petition against him, and *while insolvent*, which are held null and void as against the creditors of such debtor by the laws of the state, Territory or District in which such property is situate, shall be deemed null and void under this act against the creditors of such debtor, if he be adjudged a bankrupt," etc.

In general, then, it would appear that, where the action is brought under favor of the general provisions of § 70 or under the first clause of § 67 (3), insolvency is not a requisite element, though generally necessary in practice as a matter of evidence to establish fraudulent intent.

Obiter, *Spencer v. Nekemoto*, 24 A. B. R. 517 (D. C. Hawaii): "Under the allegation that the payment to Nekemoto was made with the intent to hinder, delay and defraud his creditors, proof of insolvency is not essential, under § 67 (e), covering this point, although insolvency would appear to be generally an existing condition where there is an attempt to defraud creditors."

§ 1216. **Transfer Itself Creating the Insolvency.**—The insolvency may have been created by the transfer itself.⁸

Spencer v. Nekemoto, 24 A. B. R. 517 (D. C. Hawaii): "If he was not insolvent then, his payment of these notes made him so and would seem to have brought his case within Bankruptcy Act, § 67 (e)."

§ 1217. **Complicity of Transferee to Be Shown.**—Unless complicity of the transferee in the fraudulent intent be shown, proof of the debtor's fraudulent intent alone is insufficient;⁹ unless the action be brought under Bankr. Act, § 67 (e).^{9a}

8. Compare, analogously, § 1344; also, see *Phillips, Trustee, v. Kleinman*, 23 A. B. R. 266 (Pa. Com. Pleas).

9. In *re Rosenberg*, 10 A. B. R. 801 (D. C.); *Laundy v. Nat'l Bk.*, 11 A. B. R. 223 (Sup. Ct. Kans.); compare, *Barker v. Franklin*, 8 A. B. R. 468, N. Y. Supp. 205; obiter, *Jacobs v. Van Sickles*, 11 A. B. R. 470, 127 Fed. 62 (C. C. A. N. J.); obiter and inferentially, *McNulty v. Wiesen*, 12 A. B. R.

342, 130 Fed. 1012 (D. C. Penn.). Cases under act 1 of Acts of Bankruptcy would be pertinent here. Compare *In re Gillette*, 5 A. B. R. 119, 104 Fed. 769 (D. C. N. Y.); obiter, *McAtee v. Strobe*, 26 A. B. R. 151, 185 Fed. 442 (C. C. A. Mo.). Intermediate transferee and transferror made party, *Phillips, Trustee, v. Kleinman*, 23 A. B. R. 266 (Pa. Com. Pleas).

9a. See post, § 1494.

Bush v. Export Storage Co., 14 A. B. R. 142, 138 Fed. 914 (D. C. Tenn.): "It may be affirmed to be true, as a general proposition, that under any State system of jurisprudence it is necessary, in order to set aside a conveyance or transfer of property as fraudulent against creditors, that the fraud must have been participated in by the vendee or purchaser as well as the vendor. If there are some exceptions, or apparent exceptions, they are not important."

The fact that the creditors have taken no affirmative or independent action to collect their claims, but simply have accepted the advantages which the fraudulent debtor has voluntarily given them for his own purposes and as a part of the fraudulent scheme, does not dispense with the necessity of proving participation of the transferee in the intent.¹⁰

And the transferee will not necessarily be exonerated by the fact that he shared the transferor's belief that the transfer, though it might delay creditors for the present, yet in the end would enable the debtor to pay all debts and extricate himself safely.¹¹

The transferee need not, however, be an active participant in the fraud.¹²

If however, the transfer were made within the four months preceding bankruptcy, then, under § 67 (e), proof solely of the bankrupt's fraudulent intent is sufficient to make a prima facie case, it being matter of defense to prove the transfer to have been made in good faith and for a presently passing consideration.¹³

§ 1218. Transferee Innocent but Consideration from Him Purely Executory.—If the transferee be entirely innocent yet the consideration moving from him be wholly executory, as, for example, a mere promise to do something at a future time not yet arrived, it has been held that the fraud of the transferor alone will suffice to avoid the transfer, and the trustee may recover the property transferred.^{13a}

Kurtz v. Troll, 175 Mo. 506, 75 S. W. 386; "Nor could he acquire a valid title, it, after such a sale, but before payment of the price, he learned of said fraud

10. *Wright v. Sampter*, 18 A. B. R. 354, 152 Fed. 196 (D. C. N. Y.).

11. *In re Elletson Co.*, 23 A. B. R. 530, 174 Fed. 859 (D. C. W. Va.), quoted ante, § 1209.

12. Instance, *Kirkpatrick v. Johnson*, 28 A. B. R. 291, 197 Fed. 235 (D. C. Pa.).

13. See post, "Fraudulent Conveyances within Four Months of Bankruptcy," § 1493, et seq. In addition, see *Smith v. Mutual Life Ins. Co.*, 19 A. B. R. 707, 158 Fed. 365 (D. C. Mass.), quoted at § 1218.

Sales of Merchandise in Bulk.—In the absence of any statute governing sales of merchandise in bulk, such a sale, though made within four months and whilst insolvent, will not be set aside if not made with the transfer-

ee's participation in the fraudulent intent. *Shelton, Trustee, v. Price*, 23 A. B. R. 431, 174 Fed. 891 (D. C. Ala.).

Reorganized Corporation Composed of Bondholders and Directors Purchasing in Assets.—*In re Medina Quarry Co.*, 24 A. B. R. 769, 179 Fed. 929 (D. C. N. Y.).

13a. Such was the ruling where an insolvent debtor paid a lump sum for an annuity to begin at a future time not yet arrived. *Smith v. Mutual Life Ins. Co.*, 19 A. B. R. 707, 158 Fed. 365 (D. C. Mass.), affirmed, S. C., 24 A. B. R. 514, — Fed. —, but this case was reversed sub nom. *Insurance Co. v. Smith*, 25 A. B. R. 768, 184 Fed. 1 (C. C. A. Mass.), though this point was held not to be necessary to the decision of the Circuit Court of Appeals.

and failed to withhold payment, provided his obligation to pay had not become so fixed or otherwise that he could not legally resist its enforcement. It needs only a simple application of these principles to settle the rights of the parties to this suit."

Blanchard v. Tyler, 12 Mich. 339, 86 Am. Dec. 57:" We are strongly inclined to think, from the testimony of Hearse himself, who was sworn in his own behalf, that he was well aware of the nature of the title, and of the attempted fraud of Tyler, and that he took the conveyance for the very purpose of aiding Tyler in the perpetration of the fraud upon the complainant. But whether he did so or not, or whether he had full notice at the time, is immaterial. He paid nothing to Tyler at the time. Tyler was owing him, he says, seven dollars and fifty cents which was to apply on the purchase, and he gave him a note, not negotiable, for \$600, less the last mentioned sum. This note, it was understood, should be paid by turning out other notes. This, it is claimed, was done, but not till some considerable time afterwards. Yet he admits that immediately after the sale to him he was fully informed of the nature of the title. Whatever he paid, therefore, was after such notice; and such payment, if in fact any notes of value were turned out, was made in his own wrong and he must bear the loss."

Haughwout v. Murphy, 21 N. J. Eq. 118: "It is held that a bona fide purchaser without notice is only protected so far as the purchase money is actually paid before notice. That securities have been given for the payment is not sufficient to protect him."

Kitteridge v. Chapment, 36 Iowa 348: "An actual payment given is necessary to the character of a subsequent bona fide purchaser for value and giving a security or existing bond or other obligation for payment is not sufficient. (Cases cited.) In holding that actual payment is generally necessary to the character of a purchaser for value, we do not mean to decide that where the purchaser has executed negotiable securities which have been actually negotiated, so as to render him liable thereon, to the holder, he would not, in such case be entitled to protection as a bona fide purchaser, but that actual payment, or what is equivalent thereto, before notice, is indispensable to the character of a purchaser for a valuable consideration."

§ 1219. Lien, Actually and Not Merely Constructively Fraudulent as to Part, Void as to All.—A mortgage or other lien actually, and not merely constructively, fraudulent and void, as to a part of the property covered by it, is void as to the whole.¹⁴

§ 1220. Fraudulent Transfer Not to Be Confused with Preferential Transfer.—Fraudulent intent is not to be confused with preferential intent, nor a fraudulent transfer with a preference.¹⁵ But an apparently

14. *Skillen v. Endelman*, 11 A. B. R. 766, 39 Misc. 261, 79 N. Y. Supp. 413.

15. *McAtee v. Shade*, 26 A. B. R. 151, 185 Fed. 442 (C. C. A. Mo.). See ante, chapter 2, § 113. And see post, "Second Element of Preference," § 1305. But compare, *In re Hill*, 15 A. B. R. 499, 140 Fed. 984 (D. C. Calif.). Also, see (*Van Iderstine*) *Trustee v. Natl. Discount Co.*, 23 A. B. R. 345, 174 Fed.

518 (C. C. A. N. Y.); also, *Coder v. Arts*, 213 U. S. 223, 22 A. B. R. 1, quoted post at § 1498.

Insolvent Corporation Giving Trust Deed to Secure Preferred Stockholders—Void though Not a Transfer to a Creditor.—*Spencer v. Smith*, 29 A. B. R. 120, 201 Fed. 647 (C. C. A. Colo.), void although, not being to a creditor, the transfer could not be a "preference" under the Bankruptcy Act.

merely preferential transfer may turn out to be a fraudulent transfer by proof of a secret trust.¹⁶

Van Iderstine v. National Discount Co., 29 A. B. R. 478, 227 U. S. 575: "Conveyances may be fraudulent because the debtor intends to put the property and its proceeds beyond the reach of his creditors; or because he intends to hinder and delay them as a class; or by preferring one who is favored above the others. There is no necessary connection between the intent to defraud and that to prefer, but inasmuch as one of the common incidents of a fraudulent conveyance is the purpose on the part of the grantor to apply the proceeds in such manner as to prefer his family or business connections, the existence of such intent to prefer is an important matter to be considered in determining whether there was also one to defraud. But the two purposes are not of the same quality either in conscience or in law, and one may exist without the other. The statute recognizes the difference between the intent to defraud and the intent to prefer, and also the difference between a fraudulent and a preferential conveyance. One is inherently and always vicious; the other innocent and valid, except when made in violation of the express provision of a statute. One is *malum per se* and the other *malum prohibitum*,—and then only to the extent that it is forbidden. A fraudulent conveyance is void regardless of its date; a preference is valid unless made within the prohibited period. It is therefore not in itself unlawful to prefer, nor fraudulent for one, though insolvent, to borrow in order to use the money in making a preference. So that, even if the Discount Company knew that Fellerman borrowed the money in order to pay off an honest debt the transfer would not have been subject of attack by the trustee, except for the fact that a petition in bankruptcy was filed within four months thereafter. But the institution of such proceedings did not relate back and convert a lawful transfer into a fraudulent conveyance."

§ 1221. Mortgages Withheld from Record.—Mortgages purposely withheld from record in order to give false credit are void in bankruptcy as against the trustee, where void by state law.

Mortgages eventually filed before bankruptcy, but withheld for a period from record by agreement for the purpose of giving credit, are void in bankruptcy, where void under the State law.¹⁷

Compare, *Rogers v. Page*, 15 A. B. R. 502, 140 Fed. 596 (C. C. A. Tenn.): "The mere fact that a mortgage has, by negligence been omitted from registration does not avoid it as between parties. But there is a distinction between a mere negligent failure to record a mortgage or deed and a deliberate agreement to do so, although the mere fact of an agreement to withhold from record is not

16. *Obiter*, (*Van Iderstine*) Trustee, *v. Natl. Discount Co.*, 23 A. B. R. 345, 174 Fed. 518 (C. C. A. N. Y.).

17. *Obiter*, *In re Ronk*, 7 A. B. R. 31, 111 Fed. 154 (D. C. Ind.). See note to *In re Wright*, 2 A. B. R. 368, 96 Fed. 187 (D. C. Ga.); inferentially and *obiter*, *In re Ewald & Brainard*, 14 A. B. R. 269, 135 Fed. 168 (D. C. Iowa). Compare, inferentially, where

it does not appear the withholding was for the purpose of giving credit, however, *Gove v. Morton Trust Co.*, 12 A. B. R. 297 (N. Y. Sup. Ct. App. Div.); compare also, *In re Shaw*, 17 A. B. R. 205 (D. C. Me.); *In re Hickerson*, 20 A. B. R. 682, 162 Fed. 345 (D. C. Idaho); *In re Wade*, 26 A. B. R. 169, 185 Fed. 664 (D. C. Mo.); *In re Duggan*, 25 A. B. R. 479, 183 Fed. 405

of itself such evidence of a fraudulent purpose as to constitute fraud in law. It is, however, a circumstance constituting more or less cogent evidence of a want of good faith, according to the particular situation of the parties and the intent as indicated by all of the facts and circumstances of the particular case."

Obiter, *Mattley v. Wolfe*, 23 A. B. R. 673, 175 Fed. 619 (D. C. Neb.), reversed on other grounds, *Mattley v. Geisler*, 26 A. B. R. 116, 187 Fed. 970 (C. C. A.): "This mortgage was not recorded for over eight months after it was given, and this was pursuant to an agreement that, because it would injure the mortgagor's credit, the mortgage was not to be filed unless the mortgagor was about to get into difficulty with his creditors, in which case the mortgagor was to notify Wolfe, so that he might file his mortgage. About seven months before his adjudication as a bankrupt, Parker had also given a chattel mortgage to one McWhinney on his stock of goods and fixtures to secure a note given by him for money loaned to him by McWhinney. This mortgage was withheld from record pursuant to a similar agreement between the mortgagor and mortgagee that, because it would injure Parker's credit, the mortgage was not to be filed except in case some creditor threatened trouble. The note and mortgage were twice renewed, and substantially the same understanding was had between the mortgagor and mortgagee with reference to the filing of these renewal mortgages. By § 67a of the Bankruptcy Act * * *: Claims which for want of record or for other reasons would not have been valid liens as against the claims of the creditors of the bankrupt shall not be liens against his estate. The validity of the claim which is thus to be tested is determined by law of this State. * * * Such an agreement between the mortgagor and mortgagee, under the decisions of the Supreme Court of Nebraska, renders the mortgage fraudulent as to certain creditors. Those creditors who can avoid the mortgage as fraudulent are those who have been misled by the keeping of the mortgage from record, and during the interim between its execution and recording have extended credit to the mortgagor on the faith that the mortgagor was the owner of such property. * * * There is no proof in this case that any creditors extended credit to Parker during the time the mortgages were withheld from record or in the belief that he was the owner of the property mortgaged."

But in Iowa, Kentucky and probably other states there must be showing made that it was withheld by agreement or that prejudice resulted from the withholding.¹⁸ And such mortgages are void in Georgia only as to innocent parties becoming creditors meantime.¹⁹

(C. C. A. Ga., affirming 25 A. B. R. 105); *In re Duggan*, 25 A. B. R. 105, 183 Fed. 405 (D. C. Ga.).

Instance where withholding of chattel mortgage for eleven months under agreement not to file because filing would lessen saleability, held not improper. *Dougherty v. First Natl. Bk.*, 28 A. B. R. 263, 197 Fed. 241 (C. C. A. Ohio).

Withholding Itself, Whether Evidence of Intent to Defraud.—Compare *McAtee v. Shade*, 26 A. B. R. 151, 185 Fed. 442 (C. C. A. Mo.).

18. *Deland v. Miller*, 11 A. B. R. 744, 119 Iowa 368; *In re Doran* (Moor-

man v. Beard), 18 A. B. R. 760, 154 Fed. 467 (C. C. A. Ky.).

19. *Bean v. Orr*, 25 A. B. R. 400, 182 Fed. 599 (C. C. A. Ga.), reversing 24 A. B. R. 434; *Clayton v. Exchange Bk.*, 10 A. B. R. 173, 121 Fed. 630 (C. C. A. Ga., reversing *In re Josephson*, 8 A. B. R. 423, 116 Fed. 404); impliedly, *In re Williams*, 9 A. B. R. 733, 120 Fed. 34 (D. C. Ga.). Compare, *In re Atlanta News Pub. Co.*, 20 A. B. R. 193, 160 Fed. 519 (D. C. Ga.). Likewise, apparently in Iowa. Compare, *Post v. Berry*, 23 A. B. R. 699, 175 Fed. 564 (C. C. A. Iowa).

Though both chattel and real estate mortgages are equally void if withheld to give false credit, yet a distinction is to be noted between them as to the necessity for showing such fraudulent intent; for even without the aid of the Amendment of 1910 "arming the trustee with process," in some states a chattel mortgage is void if merely withheld, whilst in most of the states the mere withholding of a real estate mortgage is not sufficient unless it be done with intent to obtain credit or unless some other fraudulent intent exists. Thus, in New York it is unnecessary to show the withholding of a chattel mortgage to have been done with fraudulent intent or that prejudice resulted, for such withholding, of itself, makes the mortgage void, unless it is explained as necessary;²⁰ whilst, in the same state, as to real estate mortgages it further must be shown that the withholding resulted in inducing credit, so as to estop the mortgagee.²¹

In *re Hunt*, 14 A. B. R. 416, 139 Fed. 283 (D. C. N. Y.): "In short, it is not made to appear that the nonfiling of the mortgage either induced any person to give credit to Hunt or forbear suit or bankruptcy proceedings. If the evidence established that Honeywell, president of the bank, mortgagee, kept secret and withheld the mortgage from record for the purpose of allowing the four months to run so as to defeat the provisions of the Bankruptcy Act relating to preferences, and intended so to do when he took it, this court would hold that such acts were in fraud of the Act and rendered the mortgage void. * * *

"I cannot find from this evidence that the failure to record the mortgage was accompanied by such acts on the part of the mortgagee or of its agents that a fictitious credit was given to Hunt, now the bankrupt, or that the acts of the defendant induced any creditor to forego any right. The defendant is not estopped from asserting the mortgage."

But such mortgages are not void in some states unless actual fraudulent intent is proved²² or actual levy has been made by some creditor before record;²³ and are void, in South Carolina, only as to parties becoming creditors in the meantime, but as to them are void whether they be simple contract creditors or levying creditors.²⁴

In other states, a mortgage withheld from record is void as against a

20. *Skelton v. Codington*, 15 A. B. R. 810, 185 N. Y. 80; *Korst v. Gane*, 136 N. Y. 316. Compare, on the facts, to same general effect, *In re Schiebler*, 21 A. B. R. (209) 309, 165 Fed. 363 (D. C. N. Y.); *In re Furniture Co. (Metropolitan Store & Saloon Fixture Co.)*, 15 A. B. R. 119 (Ref. N. Y.).

Thus, a chattel mortgage withheld from record for only three months and through the carelessness of an attorney was held absolutely void as against the receiver in bankruptcy. *In re Schmidt*, 24 A. B. R. 687, 181 Fed. 73 (C. C. A. N. Y.).

21. *Butcher v. Werksman*, 30 A. B. R. 332, 204 Fed. 330 (D. C. N. Y.).

22. *In re Loon*, 20 A. B. R. 719, 162 Fed. 575 (D. C. Me.).

23. *In re Shirley*, 7 A. B. R. 299, 112 Fed. 301 (C. C. A. Ohio, affirming *In re Schmitt*, 6 A. B. R. 150, cited in *Dolle v. Cassell*, 14 A. B. R. 59, C. C. A. Ohio). Similarly, *In re Wright*, 2 A. B. R. 368, 96 Fed. 187 (D. C. Ga.), where the recording was even done within the four months. *Rogers v. Page*, 15 A. B. R. 505, 140 Fed. 596 (C. C. A. Tenn.).

24. *Simmons v. Greer*, 23 A. B. R. 443, 174 Fed. 654 (C. C. A. S. Car.), quoted at § 1225½.

creditor becoming such after the execution and before the recording, whether such creditor be "armed with process" or not; and the trustee succeeds to such right.²⁵

And where withheld from record, but not by agreement with the mortgagor, the mortgage may not be void;²⁶ but, at any rate, the withholding from record is a circumstance to be considered as indicating fraud.²⁷ And the failure to record a deed given as security where invalid by State law is invalid in bankruptcy.²⁸

And the renewing of a real estate mortgage by giving a new one within every six months in order to comply with a statute requiring recording within six months of the date of execution, but the keeping of the entire series of renewals off the record, is a fraudulent scheme and is void as to creditors and the trustee, although the last renewal was recorded within the six months of its execution and before bankruptcy.²⁹

But in one case, a real estate mortgage which was not recorded until after the mortgagor's bankruptcy, but had not been withheld to give false credit, was held good.³⁰ And chattel mortgages so withheld are, "a fortiori," void as against the trustee, where void by state law as against simple contract creditors who become such during the interval.³¹

Obiter, McAtee v. Shade, 26 A. B. R. 151, 185 Fed. 442 (C. C. A. Mo.): "That the mortgage would be void as to those creditors, if any, who extended credit to the bankrupt after it was made and before it was recorded, seems clear."

In re Wade, 26 A. B. R. 169, 185 Fed. 664 (D. C. Mo.): "But failure to record may be cured as to prior creditors—that is to say, those existing at the time the mortgage was given—if the mortgagee take the property into his possession before such creditors have thus intervened, and, in that case, no lien in favor of such creditors is impressed upon the property in the hands of the trustee.

"But not so in the case of subsequent creditors; that is to say, those whose rights have intervened between the giving of the mortgage and its admission to record. As to such creditors the mortgage is absolutely void, and an equity in favor of such creditors is impressed upon the property which follows it into the hands of the trustee in bankruptcy.

^{25.} *In re Martin*, 23 A. B. R. 151, 173 Fed. 597 (C. C. A. Mo.); see also, § 1265; *obiter, McAtee v. Shade*, 26 A. B. R. 151, 185 Fed. 442 (C. C. A. Mo.), quoted *supra*.

^{26.} *In re Evans Lumber Co.*, 23 A. B. R. 881, 176 Fed. 643 (D. C. Ga.).

^{27.} *Mitchell v. Mitchell*, 17 A. B. R. 388 (D. C. N. Car.); *In re Hickerson*, 20 A. B. R. 682, 162 Fed. 345 (D. C. Idaho); *Orr v. Park*, 25 A. B. R. 544, 183 Fed. 683 (C. C. A. Ga.).

^{28.} *Dulaney v. Morse*, 29 A. B. R. 275 (Sup. Ct. Dist. Columbia).

Deed, Given as Security, Withheld under Agreement Not to Take Effect as Delivered Until Recorded.—*Ragan*

v. Donovan, 26 A. B. R. 311, 189 Fed. 138 (D. C. Ohio).

^{29.} *In re Noel*, 14 A. B. R. 715, 137 Fed. 694 (D. C. Md.).

^{30.} *In re McIntosh*, 18 A. B. R. 169 (C. C. A. Calif.). See also, *post*, § 1508. They are not void under § 67 (a) for "want of record," but, if void at all, are void for "other reasons," under § 67 (a) or as fraudulent transfers under § 70 (e), or as transferable property under § 70 (b) (4). Compare, *Gove v. Morton Trust Co.*, 12 A. B. R. 297 (N. Y. Sup. Ct. App. Div.).

^{31.} *In re Furniture Co. (Metropolitan Store & Saloon Fixture Co.)*, 15 A. B. R. 119 (Ref. N. Y.).

"The fact that the general creditor may, subsequent to the origin of his debt, receive notice of a secret mortgage, will not destroy his right which accrued prior to the notice. The creditor does not have to show that he was injured by the concealment of the mortgage; the statute assumes injury and deception and itself avoids the mortgage. The mortgagor need not have a fraudulent intent, as the statute requires no such condition. Taking possession after fraud is committed will not nullify it. So that the statute exactly meets and fully protects one who extended credit to a mortgagor in possession of the property and the mortgage not recorded."

But the debt itself may be proved, if otherwise valid, the claim upon the withheld mortgage being waived,³² or being adjudicated invalid.³³

And such withholding is held to operate by way of estoppel, even as against creditors not "armed with process" the mortgagee being estopped from asserting his lien by virtue of having given false appearance of ownership.

Clayton v. Exch. Bank, 10 A. B. R. 173, 121 Fed. 630 (C. C. A. Ga.): "Up to the very moment that Josephson filed his petition in bankruptcy, both he and the bank, so far as actions could speak—and they often speak more forcibly than words—asserted that the property of the former was not mortgaged. Both seemingly profited by this course. It seems to us inequitable to permit the bank at the last moment to produce the mortgages, and contradict the assertions made by the conduct of both the mortgagor and the mortgagee, to the injury of those who were misled and deceived. It has been said that, if one is silent when he should speak, he will not be permitted to speak when he should be silent; and is it not also just to say that if one, for improper motive, refuses to claim openly under a mortgage when duty to others requires him to do so, he shall not be permitted to assert such claim when justice to others forbids?"

In *re Tysor-Cheatham Mercantile Co.*, 24 A. B. R. 434, 178 Fed. 733 (D. C. Ga.): "Now, is it not true, in view of that reasoning, that if the general creditors—the unsecured creditors of the mercantile corporation here—knew at the very moment of its organization it had conveyed away by mortgage, not only the storehouse in which the business was to be conducted; that it had no other property, that all credit would have been refused? I think there can be scarcely a doubt of it. And if the paper is treated as a mortgage, so far as the rights of subsequent creditors are concerned, that mortgage ought to have been put upon the record, so that they would have the constructive notice of its existence. This seems wise; otherwise, men might be induced to part with their values to irresponsible purchasers, when, if the instruments had been properly registered, they could examine the records in the clerk's office and ascertain whether or not the would-be purchaser had that degree of solvency which he claimed to have."

Whether further proof must be made that the withholding actually did cause the giving of credit in reliance upon the appearance of unrestricted

32. In *re Ewald & Brainard*, 14 A. B. R. 267, 135 Fed. 168 (D. C. Iowa).

Fraudulent Transferee's Claim on

Setting Aside or Surrender, Whether Allowable.—See ante, § 774½.

33. *Post v. Berry*, 23 A. B. R. 699, 175 Fed. 564 (C. C. A. Iowa).

ownership, such as proof of a search of the public record, is to be decided in accordance with the state law.

§ 1222. Conditional Sales Contracts Withheld from Record.—Conditional sales contracts purposely withheld from record to give credit follow the same rules applicable to chattel mortgages, where subject to such rules by State law. Thus they are void in Maine.

In *re Perkins*, 19 A. B. R. 134, 155 Fed. 237 (D. C. Me.): "The facts in the case at bar disclose that the nonrecording of a 'conditional sales contract' was not a mere matter of omission. It was in pursuance of a distinct plan that there should be no record of this contract; but that the wagons should appear to be the property of the vendee. The lien was never attempted to be brought to light until after the failure of the bankrupt and his voluntary assignment. The vendee was put into possession of the wagons, of which he was apparently the absolute owner. * * * He also cites *York Manufacturing Co. v. Cassell*, supra, in which the decision is based somewhat upon *Thompson v. Fairbanks*, 196 U. S. 516, 13 Am. B. R. 437, 25 Sup. Ct. 660, 49 L. Ed. 577. In that case, in speaking for the Supreme Court, Mr. Justice Peckham said: 'Under the present Bankrupt Act the trustee takes the property of the bankrupt, in cases unaffected by fraud, in the same plight and condition that the bankrupt himself held it, and subject to all the equities impressed upon it in the hands of the bankrupt, except in cases where there has been a conveyance or incumbrance of the property which is void as against the trustee by some positive provision of the act.' But the case at bar is not 'unaffected by fraud.' The facts bring it distinctly within the rule given by Judge Wallace in *re Garcewich*, supra. In coming to a conclusion, the court gets little assistance from the line of cases which hold that, in equity, for certain purposes, the trustee merely stands in the shoes of the bankrupt, and takes all property subject to valid liens; for the case at bar does not disclose a 'valid lien,' but rather an attempted lien which is invalid and fraudulent."

And in *Georgia*.³⁴

§ 1222½. Likewise, Equitable Liens and Powers of Sale Where Held Fraudulent in Other Cases than Mortgages or Conditional Sales.—An "equitable lien" which involves the apparent ownership in one person who sells in the ordinary course of trade, will not be sustained as against the trustee, where it would work a fraud upon the law.³⁵

In *re Liberty Silk Co.*, 18 A. B. R. 582, 152 Fed. 844 (D. C. N. Y.): "But, under the authority of the same decision [*Hewitt v. Berlin Machine Wks.*] it is asserted that, inasmuch as the trustee has no better right or title to the bankrupt's property than belongs to the bankrupt or to his creditors at the time when the trustee's title accrues, the contract of August 25th, 1905, should be regarded as conferring

³⁴. In *re Braselton*, 22 A. B. R. 419, 169 Fed. 960 (D. C. Ga.).

³⁵. In *re Bellevue Pipe & F'dy Co.*, 22 A. B. R. 97, 16 Ohio D. C. 247 (Ref. Ohio).

See ante, § 1150, for cases where

equitable liens sustained as not being fraudulent, so that trustee stands in bankrupt's shoes in relation thereto. And see post, § 1253½, where equitable liens further discussed.

an equitable lien—a something which is neither a mortgage nor a conditional sale, but a partial reservation of interest on the part of the vendor, not obnoxious to any law of the State of New York, and within the equity of the Bankruptcy Act as interpreted in the case last cited. It must be admitted that no actual fraud is shown or suspected in this transaction, and that the courts of this State have gone far in upholding the validity of hypothecations of personal property even where the goods which are hypothecated were to be turned into money by the mortgagor, bailee, or conditional vendee, provided it was also agreed that the proceeds of such sale or use were to be applied in diminution of the debt secured by the goods themselves. *Prentiss Tool, etc., Co. v. Schirmer*, 136 N. Y. 304, 32 N. E. 849, 32 Am. St. Rep. 737. But I am not aware that it has been doubted since *Southard v. Benner*, 72 N. Y., § 424, that where a right existed in a chattel mortgagor to sell the mortgaged property and use the proceeds thereof generally in his own business is (however honest in intent) a fraud upon the law. The wholesome rule is summarily stated in *Re Garcewich*, 8 A. B. R. 149, 115 Fed. 87, that when property is delivered to a vendee for consumption or sale, or to be dealt with in any way inconsistent with the ownership of the seller, the transaction cannot be upheld as a conditional sale and is a fraud upon the creditors of the vendee. That rule in my judgment applies to this case. While I think as above indicated that the transaction is really a mortgage, and as such void for want of filing, yet it makes no difference whether it be denominated in one way or another it still remains true that the filatures in question were delivered to the bankrupt with obvious intent that they should be used and consumed in the ordinary course of that bankrupt's business, and for the benefit thereof. Secret liens are to be discouraged, and where, even innocently, vendors seeking to create such liens permit so obvious a badge of fraud as here appears to exist in their contracts, they must take the legal consequences, and the matter is not bettered by a name. An equitable lien which involves a fraud upon the law is none the less obnoxious because so different in form from the better known mortgage or conditional sale as hardly to fall under either well-known category."

§ 1223. Mortgages to Cover Future Advances Good Though Made within Four Months.—Chattel mortgages to cover future advances, made within four months, are not void.³⁶

Also, equitable liens made within the four months to cover future advances, are good.³⁷

§ 1224. Fraudulent Court Orders or Judgments.—Fraudulent court orders or judgments may be attacked by the trustee;³⁸ although, of

36. In *re Durham*, 8 A. B. R. 115, 114 Fed. 750 (D. C. Md.): In this case it was held, that chattel mortgages for present advances to carry on business made and duly recorded within the four months period, are not to be held void as hindering, delaying or defrauding creditors because of oral agreement that the goods covered are to be shipped to customers furnished by a particular commission house and billed in its name and the net proceeds to be applied upon the mortgage debt. Instance, *In re U. S. Food Co.*, 15 A. B.

R. 329 (Ref. Mich.). See post, that mortgages to cover future advances are not preferences, division 3 of this chapter, subdivision "A," "Third Element of Preference," § 1319.

37. Instance, *In re Cramond*, 17 A. B. R. 23, 145 Fed. 566 (D. C. N. Y.).

38. Instance, *Stern, Falk & Co. v. Trust Co.*, 7 A. B. R. 305, 112 Fed. 501 (C. C. A. Ky.): This case was decided under allegations that it was a preference; the facts indicate even more than a preference. It was a case where an assignee for creditors, under cover of

course, not collaterally.³⁹

§ 1224½. Transfers of Exempt Property, Whether May Be Fraudulent.—It has been held that creditors may not complain of transfers of exempt property as fraudulent; that only a depletion of assets which might have been subjected by creditors can be fraudulent.⁴⁰

In re Hastings, 24 A. B. R. 360, 181 Fed. 33 (C. C. A. Mich.): "Creditors cannot complain of transfers of exempt property."

§ 1225. Subsequent Creditors.—A transfer may be avoided if made with the design of defrauding subsequent creditors, or perhaps if made with intent to defraud present creditors whose claims are subsequently paid, evidence of collusion against existing creditors under the circumstances being sufficient evidence of fraud against subsequent creditors.⁴¹

§ 1225½. Ignoring Fiction of Corporate Entity.—The doctrine of corporate entity is not so sacred that a court of equity, looking through forms to the substance of things, may not, in a proper case, ignore it to preserve the rights of innocent parties or to circumvent fraud.⁴²

Thus, where a corporation was organized to take over the assets of an insolvent in order to defeat and delay his creditors, the assets thus sold have been held recoverable despite the corporate entity.

court orders, sold out stock at a purposely low price to the brother of one of the insolvents, under an arrangement that the brother sell the stock again and from the proceeds pay certain creditors 50 per cent., and the balance to the insolvents. Compare, In re Koslowski, 18 A. B. R. 723, 153 Fed. 823 (D. C. Pa.).

39. *Frazier v. Southern Loan & Trust Co.*, 3 A. B. R. 710, 99 Fed. 707 (C. C. A. N. Car.).

40. Compare similar rule as to preferentially conveyed property, post, § 1292.

41. *Beasley v. Coggins*, 12 A. B. R. 355, 57 So. Rep. 213, 48 Fla. 213: Record of the conveyance is not notice to subsequent creditors of its fraudulent character. The fact that the conveyance complained of was recorded before the creditors became such, does not impart constructive knowledge of its voluntary or otherwise fraudulent nature: the creditor is not to suppose due consideration was lacking and that the debtor's estate was being depleted. *Prescott v. Galluccio*, 21 A. B. R. 229, 164 Fed. 618 (D. C. N. Y.).

Creditors of Corporation Organized to Take Over Business of Partnership Cannot Complain That Stock Issued to Partners Was without Consideration.—In one case the court held that

subsequent creditors of a corporation organized to take over the business of a partnership which was in reality insolvent could not complain, no rights of third parties intervening and all of the old partnership creditors having been paid. In re Alleman Hardw. Co., 25 A. B. R. 331, 181 Fed. 810 (C. C. A. Pa.), reversing 22 A. B. R. 765, 158 Fed. 119).

Rights as between Subsequent and General Creditors Where Mortgage, Voidable Only as to Subsequent Creditors Is Set Aside.—Under the Amendment of 1910 giving the trustee the rights of a creditor "armed with process," it has been held that the distinction between subsequent and prior creditors does not exist upon the setting aside of an unrecorded instrument, void under that amendment, since the trustee derives his rights from the statute and not from existing creditors. In re Farmers' Coop. Co. of Barlow, 30 A. B. R. 190, 202 Fed. 1008 (D. C. N. Dak.), quoted at § 1225¾.

42. Instance, apparently, *Ludvigh v. Am. Wollen Co.*, 19 A. B. R. 795, 159 Fed. 796 (D. C. N. Y.). Compare, *Allen v. McMannes*, 19 A. B. R. 276, 156 Fed. 615 (D. C. Wis.); *Ludvigh, Trustee, v. Am. Woolen Co.*, 23 A. B. R. 314, 176 Fed. 145 (D. C. N. Y.); In re Montello Brick Works, 23 A. B. R. 375, 384, 174 Fed. 498 (C. C. A. Pa.).

In *re* (Holbrook) Shoe & Leather Co., 21 A. B. R. 511, 165 Fed. 973 (D. C. Mont.): "Surely the law will not allow this mere form of corporate organization, a mere fiction, to be used to thwart the substance of right, and thus permit the innocent creditors to be deprived of what is theirs, but will disregard the corporate entity and hold the real parties as actually having in their hands the property which is lawfully in the custody of the law, as belonging to the bankrupt. It follows that Dunn must be regarded as but a servant and agent, running a branch store of the Holbrook Company in Helena, under the style of the Packard Shoe Company; and it must be held as established that when he purchased his shares, and put the money in the shares of the Packard Company, he was really lending money to the amount of his subscription to the Holbrook Company; and so, in fact, became a creditor of the Holbrook Company, of which organization he was also a director."

In *re* Berkowitz, 22 A. B. R. 233, 173 Fed. 1012 (D. C. N. J.): "The Berkowitz Tailoring Company was incorporated shortly before the petition in bankruptcy was filed. The bankrupt was then insolvent and conveyed all his assets to the company for an alleged consideration of \$1,500. The incorporators were the bankrupt and three of his brothers-in-law. These brothers-in-law seem to have paid into the corporation, for its capital stock, the sum of \$2,000, and the bankrupt \$25. The brothers-in-law made no inquiry concerning the quantity or value of the property transferred to the company by the bankrupt and have nothing whatever to do with the business of the company. If they did in fact pay \$2,000 into the treasury of the corporation, it is clear that their purpose was not to invest that sum in the business on their own account, but to aid the bankrupt in business that was to be treated by him as his own and not as a business in which they had any interest whatever. The corporation was intended to operate as a cloak to shield the property from seizure by the bankrupt's creditors. Obviously, it was a fraud upon the creditors of the bankrupt. The referee's orders of September 26 and 27, 1907, directing the receiver to seize the property in possession of the company, were amply sustained by the proofs, and will be confirmed."

Thus, it was held in one case that where ninety-nine per cent of the stock of a manufacturing corporation was owned by a partnership and the remainder of the stock was held by relatives of one of the partners who as officers and directors of the corporation maintained its business for the benefit of the partnership, the corporation was a mere adjunct of the firm, and upon its adjudication a receivership in the bankruptcy proceedings was extended to the property in possession of the corporation as a part of the assets of the partnership.⁴³

Again, the court disregarded the fiction of corporate entity and held that the trustee in bankruptcy of the corporation was bound by an unfiled conditional sales contract where the original purchase of the property had been made by the promoters of the corporation with the declared intent of transferring it to the corporation when organized.

York v. Brewster, 23 A. B. R. 474, 174 Fed. 566 (C. C. A. Tex.): "It may be true that notice to a promoter of a corporation is not notice to the corporation itself when formed; but where associates, who hold property sub-

⁴³. In *re* Rieger, Kapner and Altmark, 19 A. B. R. 622, 157 Fed. 609 (D. C. Ohio).

ject to a lien or under a conditional sale, combine to create a corporation to hold the property, and to which they transfer it, such associates being the only persons who have any substantial interest in the corporation, the corporation stands in no better position than that in which the associates stood. * * * To avoid a result so unjust, equity will disregard forms, ignore the corporate entity, and treat the buyers, promoters, and their associates in the enterprise as the parties really interested."

Again, the fiction of corporate entity has been disregarded to the extent of consolidating bankruptcy proceedings of a partnership, of its individual members and of a corporation owned wholly by one of the partners.⁴⁴

But such right to ignore corporate entity may be lost by laches or by the intervention of innocent third parties' rights.

In *re Alleman Hardware Co.*, 19 A. B. R. 765, 158 Fed. 119 (D. C. Pa.): "The petitioner, who is the trustee in bankruptcy of L. M. Alleman, asks that the funds realized from the sale of the assets of the L. M. Alleman Hardware Co., which is also bankrupt, be taken out of the hands of its trustees, and turned over to the petitioner to be administered and distributed as the estate of L. M. Alleman individually, whom he represents. This is based on the alleged identity of L. M. Alleman with the hardware company bearing his name, which concern, as it is charged, is nothing more than L. M. Alleman himself in corporate guise. If this were true, the transfer which is asked for might be a proper one to make, although it would still be a question whether the same result could not be reached by allowing the creditors of L. M. Alleman individually to make proof of their claims against the company and so avoid circuity. But the difficulty is that the facts are not as thus assumed. There is evidence, no doubt, from which it could be found that the arrangement by which in July, 1900, S. L. Johns and H. N. Gitt took a bill of sale from Alleman for his store stock was collusive and fraudulent as to existing creditors, on the strength of which an execution or attachment, levied on the goods, would probably have held. No move of that kind however was made, and the situation at this time is not the same, so as to give a right now to what might have been done then. Over seven years have elapsed, and other rights have come in, which are entitled to consideration here. After an intermediate partnership, bearing the same name, the L. M. Alleman Hardware Co. was incorporated in March, 1903, with the capital of \$50,000, Johns subscribing for forty-nine shares, Gitt for forty-eight shares, and Alleman, C. J. Spaulding and George D. Gitt for one share each, and to it the business and stock in trade were duly transferred. In the transaction of its business, following upon that, up to the time it became bankrupt in December, 1906, new goods were purchased by the company and new and independent indebtedness incurred therefor, a large part of which remains unpaid. The parties to whom it is due, having given credit solely to the company, can look to no one else, and must be paid, so far as they are paid at all, out of its property, which the transfer to the trustee of L. M. Alleman, which is sought, would entirely cut off. It is said, however, that laches are not to be imputed to the creditors of L. M. Alleman, in this matter, as it is only since the examination of the parties in the bankruptcy proceedings, that the fraudulent character of the transaction has been disclosed. But while the evidence to establish the fraud, which is charged, may not have

⁴⁴. *Salt Lake Valley Canning Co. v. Collins*, 23 A. B. R. 716, 176 Fed. 91 (C. C. A. Mort.).

been within reach in the same fullness, as now, the outward indications of it were certainly there, and were as well known at the time of the occurrence as at any time since. And even if the details could not have been compelled from the immediate parties, as they have been here, there is no reason why they could not have been effectively obtained from the other witnesses called, who seem to have had knowledge at least of the essential facts. It is to be noted, moreover, that the present petition is refused, not so much upon the ground of laches as out of regard for the rights of creditors of the hardware company who are clearly entitled to the first concern."

§ 1225³/₄. Distribution Among Prior and Subsequent Creditors, etc., on Setting Aside Transfers Void as to a Class.—Where a transfer, void as to a certain class of creditors under State law, has been set aside, the question as to whether the proceeds shall be shared by all creditors equally or redound solely to the benefit of those belonging to the special class, is largely a question to be determined by State law, though the decisions do not usually place it upon that ground.⁴⁵

Thus, in South Carolina, where a chattel mortgage has been withheld from the records for more than the forty days limit allowed by statute for filing only creditors who have become such during the period of the withholding may share in the proceeds.^{45a}

Simmons v. Greer, 23 A. B. R. 443, 174 Fed. 654 (C. C. A. S. Car.): "The statute of South Carolina enacts that mortgages of real or personal property shall be valid, so as to affect subsequent creditors, whether lien creditors or simple contract creditors, only when recorded within 40 days; but the subsequent recording shall operate as notice to all creditors who become such after the date of the recording. Section 2456 of the Civil Code of South Carolina of 1902. This act, therefore, creates a class of creditors who are not affected by the mortgage, while all others take rights which are subordinate to it. That class is those who have become creditors between the date of the mortgage and the date of its record, and that without regard to whether they are 'lien creditors or simple contract creditors.' If there is a fund to be distributed among creditors, and some take subordinate to a lien, and there are others who are not affected by the lien, the result must be that those who are not affected by the lien are paid first, and the lien creditor is postponed to them. The South Carolina statute governs the rights of the respective parties. By that statute, and the construction placed upon it by the South Carolina courts, the mortgage is good without recording as to the bankrupt and as to all creditors whose rights accrued prior to its execution, and it is of no effect as to those creditors, whether simple contract or lien creditors, whose rights accrued between the execution of the mortgage and its recording."

And the mortgagee is not to be regarded as one of the meantime creditors, nor may he share with those becoming creditors during the period of the withholding.

⁴⁵ *Simmons v. Greer*, 23 A. B. R. 443, 174 Fed. 654 (C. C. A. S. Car.). Quoted below. Also, compare, *Moore v. Green*, 16 A. B. R. 648, 145 Fed. 480 (C. C. A. W. Va.); also, *In re Grey*, 3

A. B. R. 647, 62 N. Y. Supp. 618. Also, see post, §§ 1266, 1738.

^{45a} Also, *In re Cannon*, 10 A. B. R. 64, 121 Fed. 582 (D. C. S. Car.).

Simmons v. Greer, 23 A. B. R. 443, 174 Fed. 654 (C. C. A. S. Car.): "The assignments of error on this appeal are in effect that the judge below should have held that Simmons, the mortgagee, was entitled to share in the fund with the subsequent creditors. This contention must be upon the theory that he was as to his debt a subsequent creditor. This, we think, is an obviously strained and untenable construction. Simmons' debt and the mortgage to secure it were created simultaneously, and the debt cannot be said to have been subsequent to the mortgage. The only sensible meaning to be given to the words 'subsequent creditors,' used in the statute, is that they are creditors who become such subsequent to the execution of the mortgage."

Probably the better rule is that, in the absence of State law to the contrary, all creditors participate pro rata, both prior and subsequent creditors.⁴⁶

In *re Kohler*, 20 A. B. R. 89, 159 Fed. 871 (C. C. A. Ohio): "The matter was referred to a special master who held that the distribution should be pro rata among all the creditors. Exceptions to his report were taken before the court below, who held that the distribution should be limited to those who were creditors at the time of the transfer, on the 22nd of August, 1901. Thus, the question has reached us. The argument in favor of the conclusion reached by the court below seems to be based largely upon what is claimed to be the law of Ohio in such case, while the master in holding the distribution should be made pro rata among all the creditors, plants himself squarely upon what he contends are the policy and provisions of the present bankruptcy law. The court below pointed out that under the finding of facts as he reads it, the transfer was only 'to the detriment of his [bankrupt's] then existing creditors,' which he regards as controlling. The court thinks it 'not harmonious with justice that persons whose legal rights have in no wise been invaded, may participate in funds arising out of the transfer, which did result in the invasion of the rights of others.' And it cannot believe that the bankruptcy law, in distributing an estate, intended to give any more rights to certain creditors than they had prior to its enactment. One object of the bankruptcy law is to prevent preferences and secure equality. The letter of the law, from which we have quoted, provides for an equal distribution. All the estate of a bankrupt is to go to the trustee. This includes preferences and property fraudulently conveyed. In our view, the strong objection to the construction of the lower court is that it provides a ready method of effectuating preferences. A man heavily in debt, and likely to go in deeper, in other words, insolvent, but yet in business, may convey a large part of his property to his wife. Having thus put out an anchor to windward, he has the satisfaction of knowing that if the conveyance stands, his wife is taken care of, but if it is set aside, the creditors existing then will be preferred over the later ones. There may be reasons why the bankrupt would like to prefer his earlier over his later creditors. If so, here is a method ready at hand for the purpose. The construction of § 67f and 67c will be found in the case of *First National Bank v. Staake*, 202 U. S. 141, 15 Am. B. R. 639. Here, certain attachments had been levied within four months. The court held they could be annulled, or the lien of the attachments could be preserved under the Bankruptcy Act, for the benefit of the estate. There was no method suggested of passing over the property covered by these attachments to the creditors who had secured them. But they

46. [1867] *Smith v. Kehr*, 7 Nat. Bankr. Reg. 97.

could be held by the trustee 'for the benefit of the entire body of creditors, that is, "for the benefit of the estate"—in other words, the statute recognizes the lien of the attachment, but distributes the lien among the whole body of creditors' (202 U. S. 146). We have examined a number of Ohio decisions, but have not found one in which the distribution of the proceeds of property transferred in fraud of creditors, recovered by a trustee in bankruptcy, directly or through others, was limited to creditors existing at the time of the transfer. The precise question does not appear to have been raised, but the rule seems to be that the title of such recovered property would be held by the trustee for the benefit of all the creditors."

But in New York it was held by some of the later bankruptcy decisions before the Amendment of 1910 to the Bankruptcy Act gave the trustee the rights of a levying creditor, that a chattel mortgage withheld from record for only three months and through the mere carelessness of an attorney was absolutely void as against the receiver in bankruptcy and that its proceeds were distributable among all creditors, whether prior or subsequent.⁴⁷

Under the law of Maryland, previously existing creditors not being hurt by the withholding of a mortgage from record, the fact that it is not recorded gives them no other nor better rights than they would have had had it been recorded, and this right is not altered by the Amendment of 1910 to § 47a (2) of the Bankruptcy Act.⁴⁸

Under the Amendment of 1910, giving the trustee the rights and remedies of a creditor "armed with process," it has been held that upon the setting aside of an unrecorded instrument the division of the proceeds shall be made alike to all creditors whether prior or subsequent.

In *re Farmers' Co-Op. Co. of Barlow*, No. 2, 30 A. B. R. 190, 202 Fed. 1008 (D. C. N. Dak): "The conditional sales contracts were never filed, and, by § 6181 of the Revised Codes of North Dakota, they were for that reason 'void as to subsequent creditors without notice, and purchasers and incumbrancers in good faith for value.' Section 47a, subd. 2, of the Bankruptcy Act, as amended in 1910, provides that trustees in bankruptcy 'as to all property in the custody or coming into the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon.' If that were important, the files in this case show that there are creditors both prior and subsequent to the date of the conditional sale contract here involved. In my judgment, however, § 47 of the Bankruptcy Act, as amended, does not depend upon any such distinction. The trustee in bankruptcy derives his rights and powers from the statute, and not from the creditors of the estate. If any creditor under the local statute can obtain priority over an unfiled or unrecorded instrument by levy of attachment or execution, the trustee in bankruptcy, under § 47 as amended, has all the rights and remedies of such creditor. The distinction between prior and subsequent creditors is confined to the decisions of a few States. By the great weight of authority seizure of the property covered by an unfiled or unrecorded instrument gives to the creditor priority over such instrument, without regard to the

⁴⁷. In *re Schmidt*, 24 A. B. R. 687, 181 Fed. 73 (C. C. A. N. Y.).

⁴⁸. Compare, In *re Riehl*, 29 A. B. R. 613, 200 Fed. 455 (D. C. Md.).

time when the credit was given. Leonard Jones, in an article on Chattel Mortgages (6 Cyc. 1068), says: 'An unrecorded mortgage leaves the property as open to seizure by creditors upon a writ of attachment or execution against the mortgagor, as if no mortgage existed.' He collects the authorities and shows that the rule confining the right to subsequent creditors is limited to a few states. See, also, *First National Bank v. Ludvigsen*, 8 Wyo. 230, 56 Pac. 995, 57 Pac. 934, 80 Am. St. Rep. 928; *Pierson v. Hickey*, 16 S. D. 46, 91 N. W. 338; *Karst v. Gane*, 136 N. Y. 316, 32 N. E. 1073.

"To hold that the trustee derives his rights from the creditors of the particular estate, instead of the statute, would greatly embarrass the administration of estates in bankruptcy. It would require first an investigation to ascertain what credit was given subsequent to the unrecorded instrument. This in mercantile cases would be a difficult inquiry, and would often require the splitting of current accounts. Again, under this interpretation, the fund arising from the property covered by the unrecorded instrument would have to be first apportioned among the subsequent creditors, to the exclusion of all other creditors, then to the lienholder, and finally to the general creditors. In *re Riehl* (D. C., Md.), 29 Am. B. R. 613, 200 Fed. 455. I do not think that Congress, by the 1910 amendment of section 47, intended such a result. A fair interpretation of the statute in the light of the weight of authority, as above pointed out, gives to the trustee all the rights of the most favored creditor under the local law, and any property thus held by the trustee becomes a part of the general estate to be apportioned among all creditors in accordance with the provisions of the Bankruptcy Act on that subject."

§ 1226. Either Property Itself or Its Value Recoverable.—Either the property or its value may be recovered from the person to whom it was transferred.⁴⁹ But, where the facts warrant it, a preferential transferee will not be charged with the depreciation of securities.⁵⁰

Or, it seems, the trustee may sell his interest therein, together with the right to recover the same.⁵¹

§ 1227. Bona Fide Holder for Value Prior to Adjudication, Protected.—But if such person was a bona fide holder for value prior to the date of the adjudication, then neither the property nor its proceeds can be recovered from him.⁵² And if he is not a bona fide holder, he is not protected.

49. Bankr. Act, § 70 (e); also see *Bush v. Export Storage Co.*, 14 A. B. R. 142, 136 Fed. 918 (U. S. C. C. Tenn.). But as to a conveyance to the bankrupt's wife it has been held the trustee may pursue the property alone and may not sue for its value. *Sheldon v. Parker*, 11 A. B. R. 152, 66 Neb. 610. This would be different, probably, in States where a married woman is treated as a feme sole. *Carpenter v. Karmow*, 28 A. B. R. 21, 193 Fed. 762 (D. C. Mass.).

50. *Ernst v. Mechanics, etc., Bank*, 29 A. B. R. 289, 201 Fed. 664 (C. C. A. N. Y.).

51. In *re Downing*, 27 A. B. R. 309, 192 Fed. 683 (D. C. N. Y.) quoted ante, § 1209.

52. Bankr. Act, § 70 (e); *Bush v. Export Co.*, 14 A. B. R. 143, 136 Fed. 918 (U. S. C. C. Tenn.); *Meservey v. Roby*, 28 A. B. R. 529, 198 Fed. 844 (C. C. A. Colo.).

Instances where person held not a bona fide holder:

1. Chattel mortgagee who knew mortgagor was selling mortgaged chattels for his own use and acquiesced therein, is not a bona fide holder and the mortgage may be set aside. *Skillen v. Endelman*, 11 A. B. R. 766, 39 Misc. 261, 79 N. Y. Supp. 413.

2. *Lawrence v. Lowrie*, 13 A. B. R. 297, 133 Fed. 995 (D. C. Mass.). See post, § 1504; *Under N. Y. Stock Corp. Law*, *Perry v. Van Norden*

Thus, the hurried purchase of an entire stock of a retail merchant at less than cost, the purchaser making no inquiries, indicates lack of good faith, although the purchaser paid the price and was actually ignorant of the seller's financial condition.⁵³

In re Knopf, 17 A. B. R. 49 (D. C. S. Car.): "Assuming then that the money was actually paid and that Sanders had no actual knowledge of or intentional participation in Knopf's fraudulent purpose with respect to his creditors, is he entitled to be protected as bona fide purchaser? It is well settled that a conveyance made for a fraudulent purpose may be set aside, and that the fraud of the vendor from whom the vendee derives his title will vitiate it if the vendee has either actual or constructive notice of the fraud, and constructive notice is such a knowledge of facts as should excite the suspicions of a man of ordinary prudence, and such as ought to have put him upon inquiry as to the reasons and motives of the vendor, which inquiry if followed with ordinary diligence would have led to the discovery of the fraudulent intent."

And, where the vendees of an unregistered conditional sale contract transferred the property to a corporation, the formation of which and the transfer to which had been the basis of the negotiations for the purchase, the conditional vendees holding the only substantial interests in the corporation, the corporation was held not to be protected as a bona fide purchaser for value, even though third parties had become interested in the purchasing corporation, the court disregarding the fiction of corporate entity in such instance.⁵⁴

It has been held under the Maine Anti-Bulk-Sales Act that, since the Act does not make bulk sales fraudulent as matter of law for failure to conform to the statutory requirements of notice, etc., a purchaser in good faith will be protected, especially where the purchase price has been paid out to creditors.⁵⁵

§ 1227 ½. Allowance of Transferee's Claim on Surrender of Fraudulent Transfer.—By the same course of reasoning by which has been derived the rule permitting allowance of claims of preferred creditors on surrender of the preferences whether such surrender be compulsory or voluntary, whether made within the year or not, it is held that a fraudulent transferee may be entitled to allowance of his claim, so far as the debt itself be valid, upon surrender of the transfer.⁵⁶

In re Clark, 24 A. B. R. 388, 176 Fed. 955 (D. C. N. Y.): "If a preferential mortgage is annulled and set aside at the suit of the trustee, the creditor, so

Trust Co., 20 A. B. R. 190 (N. Y. Ct. App.).

3. Houck v. Christy, 18 A. B. R. 330, 152 Fed. 612 (C. C. A. Kans.).

4. Obiter, Coder v. Arts, 22 A. B. R. 1, 213 U. S. 223.

53. Houck v. Christy, 18 A. B. R. 330, 152 Fed. 612 (C. C. A. Kans.). See also, ante, § 1216; post, §§ 1496, 1496½.

Reorganized corporation composed of

bondholders and directors purchasing in the assets. In re Medina Quarry Co., 24 A. B. R. 769, 179 Fed. 929 (D. C. N. Y.).

54. York Mfg. Co. v. Brewster, 23 A. B. R. 474, 174 Fed. 566 (C. C. A. Tex.), quoted at § 1225½.

55. Gorham v. Buzzell, 24 A. B. R. 440, 178 Fed. 596 (D. C. Me.).

56. See also, §§ 767¾, 1227½ and 1734½.

preferred, may thereafter prove his claim, to secure which the mortgage was given, and have it allowed. *Keppel v. Tiffin Sav. Bk.*, 197 U. S. 356, 13 A. B. R. 552; *Page v. Rogers*, 211 U. S. 575, 21 A. B. R. 496."

SUBDIVISION "B."

TRANSACTIONS VOID AS TO EXISTING CREDITORS UNDER STATE LAW, TRUSTEE TAKING WITHOUT AID OF AMENDMENT OF 1910, AND FRAUD NOT NECESSARILY INVOLVED.

§ 1227¼. Trustee's Rights without Aid of Amendment of 1910 and without Fraud Necessarily Involved.—As we have seen, where there is any transfer, incumbrance or holding of property, void as to the bankrupt's creditors or inuring to their benefit by State law for want of record or for any other reason than for fraud, (or, rather, regardless of fraud) the trustee also succeeds to the rights of any existing creditor qualified by State law to avoid it, this being one of the rights the trustee always has possessed and which he still possesses, without regard to fraud and without the aid of the Amendment of 1910.

Naturally, since the Amendment of 1910 does not create the trustee into a creditor nor arm him with process until the date of the bankruptcy, we are interested in this sub-division B of the rights of existing creditors to which the trustee is subrogated, chiefly in cases where the necessary existence of a creditor or the "arming with process" must have occurred before the trustee came upon the scene as a creditor armed with process as of the date of the bankruptcy, an illustration of which case would be that of a previously unrecorded lien which is recorded before the bankruptcy, but after some creditor's rights have attached under the State law, in which case the Amendment of 1910 would not operate to invalidate the lien. The cases under this subdivision B are of two classes, dependent upon whether the State law requires or does not require that the creditor so "existing" before the bankruptcy must also have been a "creditor armed with process" at the period when his rights are claimed to have arisen in order that the transfer or lien be invalid as to him.

§ 1227½. Where by State Law Existing Creditor before Bankruptcy Must Be "Armed with Process."—Where the State law invalidates the transaction only in the event that at some particular time a creditor armed with process was in existence, and it happens that that particular time is a date prior to the bankruptcy, then it is still requisite to such invalidity in bankruptcy, notwithstanding the Amendment of 1910, that some creditor armed with process shall have existed prior to the bankruptcy, to whose rights the trustee could be subrogated under § 67, since the trustee's rights as a creditor "armed with process" under the Amendment of 1910 do not arise until bankruptcy. Thus, those cases decided before the Amendment of 1910

holding the existence of a creditor armed with process essential to the invalidating of the transaction, would be decided the same way now notwithstanding the Amendment of 1910 where such "arming with process" would have been too late under State law had it been deferred until a day which happened to be the date of the bankruptcy. The Amendment of 1910, in other words, does not change the State law as to the necessity of an existing creditor armed with process nor the date he must be "armed" but simply creates the trustee into such a creditor and arms him as of the date of the bankruptcy, leaving cases requiring an "armed" creditor at an *earlier* date, to the law as it stood before the Amendment of 1910.

Miller v. Acid & Fertilizer Co., 21 A. B. R. 416, 211 U. S. 496 (affirming 117 La. 821): "It is obvious that if, at the time of the alleged preferential transfer to Miller, there were no other creditors of the individual estate of Guillory than Miller, under the rule laid down by the Bankrupt Act, the transfer to him of assets of the individual estate, in payment of an individual debt, did not constitute a preference. That it might have constituted a preference under the State law results from the difference in the classification made by the State law, on the one hand, and the bankruptcy law on the other. * * * As the suit by the creditors was brought within four months before the adjudication in bankruptcy [the filing of the petition?] their right to a lien or preference arising from the suit was annulled by the provisions of subdivision of § 67 of the Bankrupt law. But that section authorized the trustee, with the authority of the court, upon due notice, to preserve the lien for the benefit of the bankrupt estate, and to prosecute the suits to the end for the accomplishment of that purpose. * * * Assuming, therefore, that the trustee was properly authorized, it follows that he was entitled to preserve and enforce the privilege or lien which arose in favor of the creditors, resulting from their pending action, even although the cause of action arise from the State law, and the application of that law was essential to secure the relief sought. To the accomplishment of this end the bankrupt law was cumulative and did not abrogate the State law."

First Nat. Bank v. Staake, 15 A. B. R. 645, 202 U. S. 141 (affirming Receivers v. Staake, 13 A. B. R. 281): "This clause [§ 67 (f)] evidently contemplates that attaching creditors may acquire liens upon property which would not pass to the bankrupt if the liens were absolutely annulled, and therefore recognizes such liens, but extends their operation to the general creditors. * * * As remarked by the Court of Appeals: 'The rule that the trustee takes the estate in the same plight as the bankrupt held it, is not applicable to liens which, although valid as to the bankrupt, are invalid as to creditors.'"

Impliedly, In re Butterwick, 12 A. B. R. 537, 131 Fed. 371 (D. C. Pa.): "The trustee does not stand simply in the shoes of the bankrupt but is vested with the rights of his execution creditors."

Gove v. Morton Trust Co., 12 A. B. R. 300 (Sup. Ct. N. Y. App. Div.): "The present Bankruptcy Act differs in some respects from preceding enactments of that character, in that it gives to the trustee in bankruptcy, in addition to the rights of the bankrupt, and the authority to set aside transfers made in fraud of creditors, the right which creditors would have to take advantage of the failure to file or record a mortgage or other instrument. Here, the right of a judgment creditor to resort to the property covered by the mortgage, and hence to its proceeds, has passed to the plaintiff; and we are of opinion that as a consequence he was entitled to the judgment he prayed for."

In re New York Economical Printing Co., 6 A. B. R. 615, 110 Fed. 518 (C. C. A. N. Y.): "Subdivision 'b,' § 67 (Act of 1898), preserves for the benefit of the estate in bankruptcy a right which some particular creditor has been prevented from enforcing by the intervention of the debtor's bankruptcy. If a creditor by an execution or a creditors' bill, has secured a legal or equitable lien upon the mortgaged property before the mortgagor has been adjudicated a bankrupt, under this provision his right will or will not inure to the benefit of the estate, depending upon the time when the lien was acquired. If acquired more than four months before the commencement of the bankruptcy proceeding, his lien would inure to his own exclusive benefit; but, if acquired at any time within the four months, it would be null and void, under subdivision 'f' of the section, except as preserved for the benefit of the estate as provided in that subdivision and in subdivision 'b'."

Obiter, *Watschke v. Thompson*, 7 A. B. R. 504 (Sup. Ct. Minn.): "The adjudication in bankruptcy had the effect of dissolving the attachment against the property of the bankrupt and restoring the title of the property to the estate. When the trustee received his appointment, on Nov. 29, there was one or two courses of action open to him; to accept the result of the dissolution, and pursue the property, wherever it might be, or, upon due notice, to obtain an order preserving the benefit of the attachment, if for any purpose the interests of the estate would thereby be best conserved."

In re Baird, 11 A. B. R. 438, 126 Fed. 845 (D. C. Va.): "The power of the court, and indeed its duty to take away from the attaching creditors the benefit of their liens and give it to the trustee is found specifically in § 67f."

§ 1227³/₄. Trustee's Subrogation to Existing Creditor Not Armed with Process before Bankruptcy.—Where the State law invalidates the transaction as against any existing creditor whether armed with process or not, then the trustee will be subrogated to the right of any such existing creditor, regardless of the Amendment of 1910 arming him with process.

In several states, certain transactions, notably unrecorded liens of certain classes, are invalidated if there be any existing creditor, whether that creditor be armed with process or not; thus, in the State of New York, unrecorded chattel mortgages are void as against existing creditors whether armed with process or not and such were the holdings before the Amendment of 1910, and these holdings would still remain valid. The trustee would be entitled under § 67 (a) and (b) to avoid such liens even though the liens might have been filed before the bankruptcy.⁵⁷

Karst v. Cane et al., 136 N. Y. 316: "But a delay of six weeks in filing the mortgage is not a compliance with the act. There were no circumstances rendering so long a delay necessary. There can be no doubt that if during the delay in filing, the lien had been acquired by a creditor the mortgage as to such lien would be void. The mortgage was, however, filed before the plaintiff's judgments and executions were obtained. This did not restore the validity of the mortgage as against creditors whose debts were in existence during the default in filing the mortgage, although judgments or executions were not obtained until after the mortgage was in fact filed."

⁵⁷. See, also, *Zartman v. First Nat. Bank*, 19 A. B. R. 27, 189 N. Y. 267; In re *Doran*, 17 A. B. R. 799 (D. C. Ky.).

Skilton v. Codington, 15 A. B. R. 817, 185 N. Y. 80: "The rule that a creditor must first recover a judgment is simply one of procedure and does not affect the right. Therefore, where the recovery of a judgment becomes impracticable, it is not an indispensable requisite to enforcing the rights of the creditor."

In *re Hickerson*, 20 A. B. R. 682, 162 Fed. 345 (D. C. Idaho): "It is not thought that the rule in Idaho should be held to be different from that of New York. In case of an unfiled mortgage the statute itself in terms declares that it is void, not as against "attaching creditors" but as against "creditors." By construction, the courts add that the invalidity can be asserted only by a creditor who in some way connects himself with the property. Here, as we have seen, the requisite privity exists. See also, In *re Garcewich*, 8 Am. B. R. 149, 115 Fed. 87, 53 C. C. A. 510; In *re Standard Telephone & Electric Light Co.* (D. C.), 19 A. B. R. 491, 157 Fed. 106; In *re Perkins* (D. C.), 19 A. B. R. 134, 155 Fed. 237.

"With much confidence, the bank relies upon the doctrine of *Thompson v. Fairbanks*, 196 U. S. 516, 13 A. B. R. 437, 25 Sup. Ct. 306, 49 L. Ed. 577 and *York Mfg. Co. v. Cassell*, 201 U. S. 344, 15 A. B. R. 633, 26 Sup. Ct. 481, 50 L. Ed. 782. By these decisions, undoubtedly, the rule is established or recognized that in the absence of fraud the Bankruptcy Act does not confer upon the trustee power to attack a mortgage upon behalf of a general creditor who has secured no lien. In so holding, however, the court defines only the authority conferred upon the trustee by the Federal statute. It is not to be inferred that it would be incompetent for the State Legislature in terms to declare that a non-filed chattel mortgage shall be void as to trustees in bankruptcy, or for the State courts, interpreting existing local law, to declare such a mortgage, or a mortgage permitting the mortgagor to sell the mortgage property and apply the proceeds thereof to his own use, void as against trustees in bankruptcy, and creditors whose claims have been presented and allowed."

In *re Fish Bros. Wagon Co.*, 21 A. B. R. 149, 164 Fed. 553 (C. C. A. Kans.): "The general doctrine is that an assignee in a general assignment under a State statute is neither an innocent purchaser nor a creditor having a lien on the assigned property, but that, like a trustee in bankruptcy, he stands in the shoes of his insolvent and is possessed of no greater right. It seems, however, to be otherwise in Kansas. In *Winthorow v. Citizens' Bank*, 55 Kan. 378, 40 Pac. 639, it was held that an assignee is not merely the representative of the debtor but is also a trustee for the creditors, in whom title is vested by deed of assignment, and that an unfiled chattel mortgage is void as against the right so secured by him. The effect of the assignment in question here is to be determined by the Kansas law, and it is the same upon an unfiled contract of conditional sale as upon an unfiled chattel mortgage."

§ 1228. Alleged "Consignments," "Leases," "Agencies," "Pledges," "Bailments," Where Really Sales.—Transfers amounting to actual sales or conditional sales, when the condition is void for want of recording or otherwise, but pretended or claimed to be consignments, leases, agencies, pledges, bailments or transfers of other interests; the property passes.⁵⁸

^{58.} In *re Galt*, 9 A. B. R. 682, 120 Fed. 443 (D. C. Ills., reversed, on the facts, in 13 A. B. R. 575).

In *re Leeds Woolen Mills*, 12 A. B. R. 136, 129 Fed. 922 (D. C. Tenn.); Consignor shipping goods to himself as

consignee in care of bankrupt under circumstances indicating actual sale.

Compare, In *re Howland*, 6 A. B. R. 495, 109 Fed. 869 (D. C. N. Y.): Conditional sale with right in the conditional vendee to sell in the ordinary

In *re Levin*, 11 A. B. R. 446, 127 Fed. 886 (D. C. Pa.): "It is undoubtedly true that the form of the transaction is of little consequence if the real purpose behind it is to cover up the vendee's interest in goods that have come into his possession, and thus to enable the vendor to get an advantage over other creditors to which he is not in truth entitled. As was said by the Supreme Court of Pennsylvania in *Thompson v. Paret*, 94 Pa. 275—and this statement was approved in *Peek v. Heim*, 127 Pa. 560—"whatever the form of the agreement, if its purpose was to cover up a sale and preserve a lien in the vendors for the price of the goods, it was void as respects creditors, whether the credit were given before or after the delivery of the goods. A consignment for such object was no better than any other device."

In *re Poore*, 15 A. B. R. 176, 139 Fed. 862 (D. C. Pa.): "By express agreement, the safe is to become the property of the bankrupt upon payment of the price named, and this is practically all there is to it, which makes it nothing more or less than a sale. And neither the calling of the payments rent, nor the provision that title shall not pass, nor the other conditions by which the transaction is supposed to be hedged about, are able to make it anything else.

course of trade vests absolute title in the vendee.

In *re Dunn Hardware Co.*, 13 A. B. R. 147, 132 Fed. 719 (D. C. N. Car.): Conditional sales unfiled, but disguised under form of lease.

In *re Sheets Ptg. & Mfg. Co.*, 14 A. B. R. 668 (D. C. Ohio, affirmed sub nom. *Unitype Co. v. Long*, 16 A. B. R. 282): Conditional sale unfiled but disguised under form of lease.

In *re Martin-Vernon Music Co.*, 13 A. B. R. 276, 132 Fed. 983 (D. C. Mo., reversed sub nom. In *re Smith & Nixon Piano Co.*, 17 A. B. R. 636, C. C. A. Mo.).

In *re Rabenau*, 9 A. B. R. 180, 118 Fed. 471 (D. C. Mo.): Conditional sale disguised as bailments. Distinguished in *re Flanders*, 14 A. B. R. 27, 134 Fed. 560 (C. C. A. Ills.).

Bradley, Alderson & Co. v. McAfee, 17 A. B. R. 495 (D. C. Mo.): Conditional sale (void for lack of record) and not agency.

In *re Rasmussen*, 13 A. B. R. 462, 136 Fed. 704 (D. C. Ore.): Personal property delivered to the bankrupt for sale under contracts reserving title and containing various provisions relating to ownership and possession, which are mere contrivances to secure the purchase price: the transaction is not a conditional sale but a fraud on creditors and title vests in the trustee.

In *re Garcewich*, 8 A. B. R. 149, 115 Fed. 87 (D. C. N. Y.): Pretended conditional sale but in reality a contrivance to deceive creditors.

In *re Carpenter*, 11 A. B. R. 147, 125 Fed. 831 (D. C. N. Y.): Pretended agency.

In *re Butterwick*, 12 A. B. R. 536, 131 Fed. 271 (D. C. Penn.): Pretended conditional sale.

In *re Miller & Brown*, 14 A. B. R. 439, 135 Fed. 868 (D. C. Penn.): A pretended consignment or sale on approval.

In *re Burt*, 19 A. B. R. 123, 155 Fed. 267 (D. C. Pa.): Conditional sale disguised as bailment.

In *re Penny & Anderson*, 23 A. B. R. 115, 176 Fed. 141 (D. C. N. Y.): Sale disguised as a lease.

Ludvig, trustee v. Woolen Co., 23 A. B. R. 314, 176 Fed. 145 (D. C. N. Y.): Consignment held to be a sale. So-called consignee a corporation created for purpose of giving apparent bona fides to fictitious consignment.

In *re Agnew*, 23 A. B. R. 360 (D. C. Miss.): Pretended conditional sale but no accounting made, though recording not required by State law.

In *re Priege Paint Co.*, 23 A. B. R. 385, 175 Fed. 586 (D. C. Ala.): Pretended conditional sale but an absolute sale in fact, with no right in the seller to the proceeds nor to an accounting, but only to rest on buyer's general credit.

Pontiac Buggy Co. v. Skinner, 20 A. B. R. 206, 158 Fed. 858 (D. C. N. Y.): Pretended conditional sale, or pretended agency in vendee to hold proceeds as collateral security.

In *re Arkonia Fabric Mfg. Co.*, 18 A. B. R. 467, 151 Fed. 914 (D. C. Pa.): Pretended "lease."

In *re Landsberger*, 24 A. B. R. 107, 177 Fed. 443 (D. C. Ga.).

Parlett v. Blake, 26 A. B. R. 25, 188 Fed. 200 (C. C. A. Mo.), claimed to be

There is no occasion to be astute in upholding such instruments, which in nearly every case are intended to get around the law, and, for the mere purpose of securing the payment of the price, make that out a bailment which in the real negotiations between the parties was understood and intended to be a sale." Also see same case, 15 A. B. R. 407.

Troy Wagon Wks. v. Vastbinder, 12 A. B. R. 353, 130 Fed. 232 (D. C. Penna.): "The transfer is sought to be justified on the ground that the existing relation between the parties was one of agency only, the respondent merely taking the goods to sell on account, and turning over the proceeds after deducting his commission. Written orders on Childs & Co. are produced to verify this, signed by the respondent, in which he declares that he so receives and holds them; but this is materially qualified by the other evidence, and the court will go behind mere forms to get at the real transaction. Indeed, the orders themselves—aside from the fine print at the bottom—bear on their face the proof that they represent actual purchases, and not consignments. The goods are disposed of to the respondent for a specific price, and on definite terms of credit, with provision on most of them for a discount if paid within a certain time. And while it may be true, as stated by the respondent, that he was only required to pay for each lot as fast as he disposed of it, accounting to Childs & Co. for whatever he received in the way of notes or other securities, yet in making sales he did so in his own name, and was held directly responsible, the securities obtained being taken to himself personally, and guaranteed by him when they were turned over. His obligations to Childs & Co. were plainly regarded as a debt, and he so speaks of them in his testimony. There are too many indicia in this of an ordinary purchase, to warrant the conclusion that anything else was in fact intended."

In re Tice, 15 A. B. R. 97, 139 Fed. 52 (D. C. Pa.): "In Pennsylvania, where goods were delivered by claimant to a bankrupt, under an agreement 'to pay rent for the use of the same,' in certain installments, covering specified periods, and upon making further specified payment, not designated as rent, a bill of sale to be given, the claimant 'to have the privilege of taking' the goods 'if the rent is not paid,' the transaction is a conditional sale and not a bailment, and subjects the property to the claims of the creditors of the bankrupt.

"The general rule in Pennsylvania is that the delivery of goods, with a provision that the title shall not pass until the purchase price has been paid, is void as to creditors of the party to whom they are delivered, and the essential character of the transaction is regarded rather than the particular form assumed."

In re Wood, 15 A. B. R. 411, 140 Fed. 964 (D. C. Pa.): Sale and not bailment: "The goods were billed to the bankrupt as though it was a sale, and while this is not conclusive it is of more or less persuasive force."

Thus, transactions that amount to conditional sales or chattel mortgages are frequently claimed to be pledges where the condition of the sale is ren-

an agency bailment but held to be sale because of agreement to "buy and pay for" goods left at end of year's agency.

In re Norton, 24 A. B. R. 794, 181 Fed. 901 (D. C. Pa.), a pretended "lease."

In re Nelson, 27 A. B. R. 272, 191 Fed. 233 (D. C. S. D.); *In re Schoenfeld*, 27 A. B. R. 64, 190 Fed. 53 (D. C. W. Va.); *In re Fitzgerald*, 26 A. B. R.

710, 188 Fed. 763 (D. C. Conn.); *In re Hartdagen*, 26 A. B. R. 532, 189 Fed. 546 (D. C. Pa.); *In re Groezinger*, 28 A. B. R. 732, 199 Fed. 935 (D. C. Pa.); *Ommen v. Talcott*, 26 A. B. R. 689, 188 Fed. 401 (C. C. A. N. Y.); *In re Hinson Bros.*, 26 A. B. R. 754, — Fed. — (D. C. Ga.); *In re Franklin Lumber Co.*, 26 A. B. R. 37, 187 Fed. 281 (D. C. Pa.).

dered nugatory by failure to record the contract, or the chattel mortgage is void for want of record.⁵⁹

Of such class of subterfuges are attempted "warehousings" by insolvent debtors of their own property on their own premises, pretending the transaction to be pledges or bailments, but retaining control and substantial possession all the time.⁶⁰

Instance, *In re Rodgers*, 11 A. B. R. 79, 125 Fed. 169 (C. C. A. Ills.): "We are thus brought to the consideration of the real character and purpose of the transaction between the bankrupt and the storage company. We are to ascertain the real intention of the contracting parties from the whole agreement read in the light of the surrounding circumstances. The bankrupt was largely engaged in purchasing seed upon credit, storing the property purchased in his warehouse. He occupied the premises as a place of business, maintaining an office there, with clerks to assist in the management of the business, and with porters to handle the seed. The premises were subject to a rental of \$250 a month. He arranged with the storage company, which had no warehouse of its own, that it would issue warehouse warrants or receipts to the bankrupt for property upon the bankrupt's premises for a certain small charge per month upon the value of the property covered by the receipts. He executed a lease of the premises to the storage company, to continue so long as the bankrupt should desire, and so long as property remained therein for which warrants or receipts had been issued; and this without any payment of rent by the storage company, the rental in fact being paid by the bankrupt. The storage company neither required, nor was it given any key to the premises. The bankrupt remained in possession of the premises as before the agreement, continuing to transact his business there as he had formerly done. There were certain signs placed upon the different floors of the building, indicating that the storage company controlled the premises. These were small and obscure signs, not likely to attract attention, and most of them hidden behind the piles of bags of seed. No sign was displayed upon the exterior of the building indicating any proprietorship of the storage company, or giving notice to the world that any other than the bankrupt had possession and control. There was no open, notorious manifestation of a change of possession, none was intended and there was none in fact. Upon each pile of bags of seed for which the warehouse receipts or warrants were issued there was placed a small tag, which might be discovered upon careful search. The bankrupt substantially treated this property as his own, at times going through the forms prescribed by the storage company, and, whenever he found it necessary, ignoring them. We do not find that the storage company had knowledge of this action of the bankrupt, but it certainly knew that it was possible under the

59. *In re Rodgers*, 11 A. B. R. 79, 125 Fed. 169 (C. C. A. Ills.).

60. Compare, to same effect, ante, § 1146. *Warehousing Co. v. Hand*, 16 A. B. R. 49 (C. C. A. Wis.); *Warehousing Co. v. Hand*, 19 A. B. R. 291, 206 U. S. 415, quoted at § 1146. [Observe that *Warehousing Co. v. Hand* was affirmed by Supreme Court, 19 A. B. R. 291, 206 U. S. 415, and explicated further by Supreme Court, in *In re Standard Tel. & Elec. Co.* (Knapp v. Milw. Tr. Co.), 24 A. B. R. 761, 216 U. S. 545, quoted further at §§ 1211

and 1258.] *Fourth St. Nat'l Bank v. Millbourne Mills Co.*, 22 A. B. R. 442, 172 Fed. 177 (C. C. A. Pa., affirming *In re Millbourne Mills Co.*, 20 A. B. R. 747, 162 Fed. 988), quoted at § 1146; *In re Nelson*, 27 A. B. R. 275, 191 Fed. 233 (D. C. S. Dak.), quoted ante, at § 1146.

Instance, agency to sell with stipulation that agent shall "buy and pay for" all goods remaining unsold at end of agency year. *Parlett v. Blake*, 26 A. B. R. 25, 188 Fed. 200 (C. C. A. Mo.).

circumstances for the bankrupt to do with the property as he would, since it was left within his control. It is difficult for us to look upon this transaction as a warehousing of property. The storage company assumed no liability to the bankrupt, and assumed only such responsibility as the law imposes upon it with respect to those advancing money upon the faith of its warehouse warrants or receipts. The name of the company is in itself, under the circumstances, a false pretense. It did not store property. It had no premises upon which to store property. The bankrupt stored the property. The bankrupt paid the rental of the premises. It is true that an agent of the storage company occasionally visited the premises and inspected the property in a sort of way, but exercised no supervision or control that would prevent the bankrupt from doing with it as his will might dictate or his financial necessities might require. We cannot but regard this arrangement as a subterfuge, a mere device to enable the bankrupt to hypothecate the warehouse warrants or receipts, and so to raise money upon secret liens upon property in his possession and under his control."

Thus, likewise, unfiled conditional sales and unfiled chattel mortgages are sometimes pretended to be property held in trust.⁶¹

Again, it is often sought to make an absolute sale to the bankrupt appear to be a bailment, in order that the property may be reclaimed. But the property affected will pass if the true nature of the transaction makes it a sale.⁶²

In *re Heckathorn*, 16 A. B. R. 467 (D. C. Pa.): "It is rather suggestive of an attempt, as is said above, to have the benefit of a sale without the responsibility for it, disposing of the goods at a price and at the same time retaining a hold upon them and upon the proceeds derived from their sale. But why this beating behind the bush when a direct course was open to them? If the intention was that the bankrupt should receive and sell the goods for an account of the petitioners, upon a commission, it would have been easy, in so many words, to say so; and the failure to do it can but be regarded as significant."

Chisholm v. Earle Ore Sampling Co., 16 A. B. R. 423 (C. C. A. Colo.): "But whatever doubts arise from the face of the contract are dispelled by the conduct of the parties under it. It is a familiar rule that, where there is uncertainty as to the true meaning and intent of the contracting parties, the construction which they themselves have put upon it by their voluntary course of practice, when no controversy existed, is always to be given very great, if not controlling, effect. * * * The parties acted under the contract as though the transactions were sales of ore upon the basis of the assay value of the samples."

In *re Wells*, 15 A. B. R. 419 (D. C. Pa.): "There is no particular magic in the terms 'consigned' or 'consigned account.' In a sense all goods shipped to another

61. In *re Tweed*, 12 A. B. R. 648 (D. C. Iowa): Unfiled conditional sale. In *re Jerstman*, 17 A. B. R. 882 (D. C. N. Y.): Unfiled chattel mortgage; *Pontiac Buggy Co. v. Skinner*, 20 A. B. R. 206, 158 Fed. 858 (D. C. N. Y.): Pretended conditional sale. In *re Southern Textile Co.*, 23 A. B. R. 172, 174 Fed. 523 (C. C. A. N. Y.): Unfiled chattel mortgage, claimed to be either held in trust or under "equitable lien."

62. In *re Franklin Lumber Co.*, 26

A. B. R. 37, 187 Fed. 281 (D. C. Pa.).

Bush v. Export Storage Co., 14 A. B. R. 138, 136 Fed. 918 (U. S. C. C. Tenn.); In *re Wood*, 15 A. B. R. 411, 140 Fed. 964 (D. C. Penn.): Goods ordered for exhibition at a fair, but billed at regular prices and remaining in bankrupt's unquestioned possession for six months or more. Instance, goods actually sold and paid for, yet claimed to be consigned. In *re Landsberger*, 24 A. B. R. 107, 177 Fed. 443 (D. C. Ga.).

are consigned to him. The question is what was the inherent character of the transaction, which depends upon the purpose of it."

In *re Morris*, 19 A. B. R. 422, 159 Fed. 591 (D. C. Pa.): "It is difficult to give a written instrument a character which the transaction, which it purports to represent, does not inherently bear. While, therefore, it is easy enough to make an agreement speak as a lease or a bailment, where that was what was actually in the mind of the parties, where the fact is that the one desires to sell and the other to buy, the attempt to have the arrangement masquerade in writing as something else is very likely to fail. There are apt terms and provisions for the one, which are inapt and unadaptable for the other, and the result is a nondescript, the different parts of which defeat each other and make manifest the real purpose in view. And this is often also betrayed by the unusual little things which creep in, 'the clausulae inconsuetae pointed to in *Twyne's case*, 3 Rep. 80, as the sure badges of that which they are intended to hide.' *Taylor v. Taylor*, 8 How. 183, 205, 12 L. Ed. 1040; In *re Baxter* (C. C. A.), 152 Fed. 137, 141. As experience teaches, such instruments are prompted by the desire on the part of the owner of the goods to have the benefit of a sale while escaping its responsibilities, retaining a hold on them so as to be secure of the price, without subjecting them to claims of creditors by reason of having parted with the possession, although giving credit to the one obtaining them, in their eyes, as the apparent owner thereby. This is not the policy of the law, and there is no occasion for the courts to be astute in helping to get around it. On the contrary, the result cannot but be healthful where attempted evasions of it are brought to naught."

In *re Gehris-Herbine Co.*, 26 A. B. R. 470, 188 Fed. 502 (D. C. Pa.): "Tested, therefore, by that law, what is the true character of the contract in question? Is it a bailment, or a conditional sale? If it is really and in good faith a bailment, it is valid not only between the parties but against creditors also; for a man does not lose title to his property by hiring it to another, although, he may have parted with the possession and the other may have acquired it. But, if he has really sold it and has also parted with the possession, he will find in numerous jurisdictions—in Pennsylvania, for example—that he cannot enforce against execution creditors a condition that he has retained the title until the price is paid. These rules are too well known to need the support of citation."

In *re Gaglione & Sons*, 28 A. B. R. 694, 200 Fed. 81 (D. C. Pa.): "In looking the whole transaction over, it discloses a sale of property and not a lease by bailment. It is true that the writing constitutes a valid bailment between the parties, but they went beyond its plain terms and provisions. The purpose of the parties obviously was not to hire out, but to sell the machines. Their acts, as well as their writings, will be regarded by the court in determining the true character of the transaction. Since the amendment of § 47a (2) by the act of June 25, 1910, the trustee is placed upon the footing of a creditor with a legal or equitable lien and may take full advantage of such rights. He may, therefore, attack a contract, in form of a bailment, and offer such evidence as will throw light upon the negotiations, between the parties, disclosing its true meaning to be otherwise. * * *

"To constitute a valid bailment the intent to return the property must be evidenced by the agreement. Now, if this so appears from the writing, and it is otherwise shown conclusively that it was not so intended, a bailment is not to be presumed. In this case the intention to return is denied by the act of the parties, the delivery and acceptance of the notes in payment of the purchase price of the machinery. Such payment or security for payment, if so to be regarded, presupposes a sale and rebuts the idea of a lease. If it had been the intention of the claimant to continue his title to the property, why did he require payment

or security for such payment. That he was willing to pass title is evidenced by his act in the acceptance of the notes from the bankrupt, in the exercise of the latter's option to purchase by the terms of the writing, postponed to a future date, and having exercised his option to purchase by the consent of the claimant, title was transferred."

Thus, it is often sought to make it out to be a conditional sale.⁶³

In *re Geo. O. Haasam & Son (Flint v. Buttles)*, 18 A. B. R. 745, 153 Fed. 932 (D. C. Vt.): "In the case at bar, there was an attempted lien, absolutely secret, not even made known to the vendee, and never intended to be brought to light unless the vendee should become insolvent. The vendee was put in possession of a large number of wagons, of which he was apparently the absolute owner. There was a secret attempt on the part of the vendor, should the vendee succeed in getting credit by having about him a large amount of unencumbered property and should thereafter be unable to pay debts so incurred, to make time notes given for said property 'immediately due and payable,' and the vendee deliver to the vendor all goods remaining unsold, and all the while they should remain in the name of the vendor. I cannot conceive in what manner the vendor anticipated that the goods could remain in its name when possession was passed to the vendee and no record made of the transaction. It has been repeatedly held that when personal property is delivered to a vendee for sale, or to be dealt with in a way inconsistent with the ownership of the seller, or so as to destroy his lien or right of property, the transaction cannot be upheld as a conditional sale and is fraud upon the creditors of the vendee."

But where the transaction amounts to a bona fide consignment to the bankrupt or bailment to him, and is not a concealed sale, the trustee does not acquire title.⁶⁴

63. Instance, *In re Cohn*, 18 A. B. R. 786 (Ref. Calif.).

64. *Smith & Bro. Typewriter Co. v. Alleman*, 28 A. B. R. 699, 199 Fed. 1 (D. C. Pa.); *In re Levin*, 11 A. B. R. 446, 127 Fed. 886 (D. C. Penn.); *In re Smith & Nixon Piano Co.*, 17 A. B. R. 636 (C. C. A. Mo., reversing *In re Marten-Vernon Music Co.*, 13 A. B. R. 276).

Instance, *In re Rubber Ref. Co.*, 15 A. B. R. 72 (D. C. Penn.): Bailment with option to purchase or "Sale on Approval," with disapproval signified.

Shipment of leather; bailment not conditional sale: *In re Flanders*, 14 A. B. R. 27, 134 Fed. 560 (C. C. A. Ills.).

Subsequent "lease" of machinery, originally sold for cash but cash not paid. *Canning Machinery Co. v. Fuller*, 20 A. B. R. 157, 158 Fed. 588 (C. C. A. Ala.). Subsequent lease of property originally transferred to the bankrupt to enable him to acquire credit where credit not obtained thereby. *Nylin v. Am. Trust & Sav. Bank*, 21 A. B. R. 535, 166 Fed. 276 (C. C. A. Ill.). Instance, bailment, not conditional sale.

In re Angeny, 18 A. B. R. 491, 151 Fed. 959 (D. C. Pa.). Instance "sale on approval" or "sale and return." *In re Landis*, 18 A. B. R. 483, 151 Fed. 896 (D. C. Pa.). Instance, genuine conditional sale. *In re Max Cohen*, 20 A. B. R. 796, 163 Fed. 444 (D. C. N. Y.). Instance of sales on approval, etc., see ante, § 1145, et seq. Instance, valid conditional sale though unrecorded and without power to sell, *In re Gray*, 21 A. B. R. 375, 170 Fed. 638 (D. C. Okla.). Instance, valid conditional sale. *Reardon v. Rock Island Plow Co.*, 22 A. B. R. 26, 168 Fed. 654 (C. C. A. Ill.). Instance, contract held to be genuine bailment and not conditional sale. *Franklin v. Stoughton Wagon Co.*, 22 A. B. R. 63, 168 Fed. 857 (C. C. A. Okla.). Instance, *Walther v. Williams Mercantile Co.*, 22 A. B. R. 328, 169 Fed. 270 (C. C. A. Mich.), wherein the bailment was of an entire stock of merchandise, fixtures and business to be operated by the bailees on condition that they keep the store replenished and pay the bailors certain commissions, the bailors to

Plow (Deere) Co. v. McDavid, 14 A. B. R. 664, 137 Fed. 802 (C. C. A. Mo.): "We think it was an agency contract. It is not a contract in which the consignee can sell at any price, or on any terms he may choose, but, as we understand it, it is a contract or consignment of goods to be sold on commission by the consignee, as agent for the consignor, for cash. The plow company had the right, under the contract, to require the goods returned, and in this it lacks one of the necessary elements of a contract of sale, namely, to pay money, or its equivalent, for the goods delivered, with no obligation to return."

In *re Galt*, 13 A. B. R. 575 (C. C. A. Ills., reversing 9 A. B. R. 682): "Applying to this contract the test stated, it is clear that here was a bailment and not a conditional sale. It was not contemplated that Galt should ever own these wagons. He was to sell them to others for the company, his commissions to be the amount which he might receive over the prices stated in the contract. The proceeds, whether in cash or in notes of the purchaser, were to be immediately returned to the company, the notes being guaranteed by Galt. This was a *del credere* commission and not a sale. The company could compel a return of the goods not sold. Galt had not the option to pay for them in money. Even with respect to the goods unsold within the twelve months, the option for their return or payment was with the company and not with Galt; and nowhere in the agreement does the latter covenant to pay for these goods as in the case of a sale."

In *re Columbus Buggy Co.*, 16 A. B. R. 759, 143 Fed. 849 (C. C. A. Okla.): "A contract between a furnisher of goods and the receiver that the latter may sell them at such prices as he chooses, that he will account and pay for the goods sold at agreed prices, that he will bear the expenses of insurance, freight, storage and handling and that he will hold the merchandise unsold subject to the order of the furnisher, disclose an agreement of bailment for sale, and does not evidence a conditional sale. Such a contract is not affected by a statute which renders unrecorded contracts for conditional sales voidable by creditors and purchasers."

"An agreed price, a vendor, a vendee, an agreement of the vendor to sell and of the vendee to buy for and pay the agreed price are essential attributes of a contract of sale. The power to require the restoration of the subject of the agreement is an indispensable incident of a contract of bailment."

"The fact that a contract provides that the receiver of goods is to account for those sold at fixed prices and to retain the difference for insurance, storage, commission and expenses does not make the contract an agreement of sale."

Thus, where a contract to furnish certain articles provided that until sold or paid for in cash they should remain the property of the seller, and, when sold, all proceeds of sale including notes, accounts, etc., should be kept separate as a trust fund and be turned over to the seller or be held as collateral security, the court held the seller's rights were unimpaired by the

give the bailees a certain amount on repossession for any excess of value. Bailment, not a transfer. (*Walter A. Wood Co. v. Vanstory*, 22 A. B. R. 740, 171 Fed. 375 (C. C. A. N. Car.).

Subsequent giving of notes by consignee held not to convert consignment into absolute sale, where, notwithstanding, the consignee was required to account for goods sold. In

re Bailey, 23 A. B. R. 876, 176 Fed. 628, 176 Fed. 990 (D. C. Ga.).

In *re Reynolds*, 29 A. B. R. 145, 203 Fed. 162 (D. C. Ky.), wherein the court held that an agency contract, is not made a sale contract as to goods not sold, because on the first day of each month it became a sale contract as to the proceeds of the goods sold during the preceding month on time.

bankruptcy and that he had a right to all such notes, accounts, etc., in such fund.⁶⁵

If the seller retains full control of the disposition of the goods and may direct the goods to be returned to the seller or to be shipped elsewhere as desired, the transactions is deprived of one of the essential elements of a sale.

Franklin v. Stoughton Wagon Co., 22 A. B. R. 63, 168 Fed. 857 (C. C. A. Okla.): "Under these provisions we think the wagon company retained full control of the disposition to be made of the wagons, in that it could direct the goods returned to the house or shipped elsewhere as desired, and in this it lacks one of the necessary elements of a contract of sale, namely, to pay money or its equivalent for the goods delivered with no obligation to return."

A bailment is not a transfer, not even under the broad definition of Bankr. Act, § (25), that "transfer shall include the sale and every other and different mode of disposing of or parting with property, or the possession of property, absolutely or conditionally, as a payment, pledge, mortgage, gift or security."⁶⁶ The rule of "*noscitur a sociis*" would seem to make plain that a bailment was not of a like class with those expressly enumerated.

An executory contract of sale may be converted by verbal agreement made before delivery of the goods, later reduced to writing, into a bailment with alternative of future conversion into a sale.⁶⁷

But it has been held that an attempted conversion of an unrecorded executed conditional sale into a bailment by subsequent agreement will be ineffective.⁶⁸

In re Poore, 15 A. B. R. 407, 139 Fed. 863 (D. C. Pa.): "No doubt, while the matter was still executory, the conditions on which it was held could be readjusted. *Goss Ptg. Co. v. Jordan*, 171 Pa. 474; *Stiles v. Seaton*, 200 Pa. 114; *In re Naylor Mfg. Co.*, 14 A. B. R. 284. But not to the detriment of those creditors who either were such at the time the machinery was obtained or had become so since then, as to whom it had passed beyond the executory stage."

And the State law controls as to the real character of the transaction.⁶⁹

Bryant v. Swofford Bros. Co., 22 A. B. R. 111, 214 U. S. 279: "* * * in bankruptcy, the construction and validity of such a contract must be determined

65. *In re McGehee*, 21 A. B. R. 656, 166 Fed. 928 (D. C. Ga.); to similar effect, *Wood Co. v. Eubanks*, 22 A. B. R. 307, 169 Fed. 929 (C. C. A. N. C.); *Corbitt Buggy Co. v. Ricaud*, 22 A. B. R. 316, 169 Fed. 935 (C. C. A. N. C.).

66. (Walter A.) *Wood v. Vanstory*, 22 A. B. R. 740, 171 Fed. 375 (C. C. A. N. Car.).

67. *In re Naylor Mfg. Co.*, 14 A. B. R. 284, 135 Fed. 206 (D. C. Penn.);

In re Miller & Brown, 14 A. B. R. 443, 135 Fed. 868 (D. C. Penn.). Sale on approval; goods being disapproved and set aside for return before levy. *In re Rubber Ref. Co.*, 15 A. B. R. 72 (D. C. Penn.).

68. Effect of subsequent acceptance of notes, *In re Gray*, 21 A. B. R. 375 (D. C. Okla.).

69. *In re Burke*, 22 A. B. R. 69, 168 Fed. 994 (D. C. Ga.).

by the local laws of the States. * * * That such a contract is a conditional sale and is valid without record is the law of Arkansas."

In re Morris, 19 A. B. R. 422, 159 Fed. 591 (D. C. Pa.): "The question is one of local law in which the decisions of the State court control."

First Nat. Bank v. Guarantee Title & Trust Co., 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.): "Whether a conditional contract of sale, chattel mortgage or pledge of personal property is valid against the general creditors of the vendor, mortgagor or pledgor or his trustee in bankruptcy is to be determined by the local laws of the State in which the transaction is had."

It has been held that the subsequent giving of notes by the bankrupt would not operate to change his agency under a consignment contract nor to alter the relation of bailee and bailor, into an absolute sale, where all the evidence shows that the intention among the parties was not to make such change in the relations, and where the consignee was required to account fully for the goods actually sold notwithstanding the notes, the trustee standing simply in the bankrupt's shoes in this regard.⁷⁰

Of course, where such consignment contracts or conditional sales are held to be void by State law as a fraud upon creditors, such a reaffirmance of the continuance of the relation between the parties would not prevail as against the trustee, even before the Amendment of 1910, for in cases of fraud the trustee never has stood "in the bankrupt's shoes."⁷¹

Trustee Now "Armed with Process" by Amendment of 1910.—Wherever State law, in relation to transactions of the sort herein mentioned, would give different rights or a different construction of the facts to a levying creditor from what it would give to a mere general creditor, the trustee will have such different rights or construction.

Thus, as to a conditional sale to which an attempt has been made to give the character of a bailment.

In re Franklin Lumber Co., 26 A. B. R. 37, 187 Fed. 281 (D. C. Pa.): "In reality it has always been a contract of conditional sale although it may be true that the bankrupt himself would not have been permitted to prove its true character. Neither could the trustee have proved its true character until the Act of June 25, 1910, was passed, but since that date he has been put upon the footing of a creditor with a legal or equitable lien, and may take full advantage of such rights. Whenever therefore such a creditor may attack a contract, in form a bailment, on the ground that it is really a conditional sale, and may support the attack by competent and relevant evidence that throws light on the true meaning of the contract—the trustee has the same right. The mere form of the agreement does not bind him, as it might bind the bankrupt." This case further quoted in § 1270.

And where, under the local law, the transaction is void as to lien creditors, it is also void as to the trustee, so far as property in the custody of the bankruptcy court is concerned, by virtue of the Amendment of 1910;⁷²

⁷⁰ In re Bailey, 23 A. B. R. 876, 176 Fed. 628, 176 Fed. 990 (D. C. S. C.).

⁷¹ See ante, § 1209.

⁷² In re Appel Suit & Cloak Co., 28 A. B. R. 818, 198 Fed. 322 (D. C. Colo.).

and the trustee may now, by virtue of the amendment, attack these transactions as effectively as if he were a creditor holding a lien by legal or equitable proceedings.⁷³

§ 1228½. Disguised Conditional Sales Invalid for Lack of Record Even Though No Creditor "Armed with Process" Exists.—Before the Amendment of 1910, it was held that even if the transaction did not amount to a pledge, consignment, bailment, trusteeship, etc., but was in effect a conditional sale, unrecorded, and not an absolute sale, the trustee would not get title in most states, unless some creditor "armed with process" existed;⁷⁴ although in some states they were considered to be fraudulent, in which event the trustee was held not to be "standing in the shoes of the bankrupt;" but by the Amendment of 1910 to Bankruptcy Act, § 47a (2), the trustee is given, in effect, the rights of a creditor "armed with process."⁷⁵

Of course, if by State law an unfiled conditional sales contract is not void as against levying creditors, it would not be void as against the trustee even under the Amendment of 1910.⁷⁶

§ 1229. Liens Void as to Creditors for Want of Record, Void as to Trustee.—Claims, which, for want of record, would not have been valid liens as against the claims of any creditor of the bankrupt, are not liens against his estate.⁷⁷

§ 1230. Unrecorded or Unfiled Chattel Mortgages Void.—An unrecorded or unfiled chattel mortgage is void as against the trustee in states where recording or filing is required to preserve the lien against creditors.⁷⁸

73. In re Gaglione & Son, 28 A. B. R. 694, 200 Fed. 81 (D. C. Pa.).

74. In re Fabian, 18 A. B. R. 488, 151 Fed. 949 (D. C. Pa.).

75. See ante, §§ 1141, 1241, 1243. See also, In re Hartdagen, 26 A. B. R. 532, 189 Fed. 546 (D. C. Pa.), quoted at § 1242; In re Franklin Lumber Co., 26 A. B. R. 37, 187 Fed. 281 (D. C. Pa.).

76. Hewitt v. Berlin Machine Wks., 11 A. B. R. 709, 194 U. S. 296, quoted at § 1141; Bryant v. Swofford Bros., 22 A. B. R. 111, 214 U. S. 279, quoted at § 1141.

77. Bankr. Act, § 67 (a); obiter, In re Runk, 7 A. B. R. 31, 111 Fed. 154 (D. C. Ind.); also, see post, § 1507.

In re Buchner, 29 A. B. R. 179, 202 Fed. 979 (D. C. Ill.); In re Southern Textile Co., 23 A. B. R. 172, 174 Fed. 523 (C. C. A. N. Y.); obiter, Crucible Steel Co. v. Holt, 23 A. B. R. 302, 174 Fed. 127 (C. C. A. Ky.); In re McDonald, 23 A. B. R. 51, 173 Fed. 99 (D. C. Mass.).

Recording after Bankruptcy.—Instances, *Hanson v. Blake*, 19 A. B. R.

325, 150 Fed. 342 (D. C. Me.); In re Burlage Bros., 22 A. B. R. 410, 169 Fed. 1006 (D. C. Iowa); "Of course the record of the instrument after the bankruptcy could avail nothing." See further, § 1270, et seq., as to the effect of the Amendment of 1910.

78. In re Nuckols, 29 A. B. R. 867, 201 Fed. 437 (D. C. Tenn.); In re Jules & Frederic Co., 27 A. B. R. 136, 193 Fed. 533 (D. C. Mass.); In re Forse, 25 A. B. R. 134, 182 Fed. 212 (D. C. N. Y.); Title Guar. & Surety Co. v. Witmire, 28 A. B. R. 235, 195 Fed. 41 (C. C. A. Mich.), decided under the law of Minnesota.

As to chattel mortgages void for other faults than nonrecord, see In re Hammond, 26 A. B. R. 336, 188 Fed. 1020 (D. C. Ohio), quoted at § 1270.

The same ruling has been made as to a bill of sale held as security. *Marden v. Phillips*, 4 A. B. R. 566 (D. C. Mass.). Also, see §§ 1209, 1257, 1270.

Recording Part of Instrument.—Failure to record entire contract prevents record of part from operating as

It has been held that the recording of mortgages of chattels real is to be governed by the recording laws relating to mortgages and conveyances of real property, and not those relating to the recording of chattel mortgages.⁷⁹ Thus, an unrecorded chattel mortgage upon a vessel derrick hoister has been held void.⁸⁰

§ 1231. Unfiled Chattel Mortgages Not Void Where Filing or Recording Not Required.—And unfiled chattel mortgages are not void where filing or recording is not required by the State law in order to make them valid as against levying creditors.⁸¹

In *re Josephson*, 8 A. B. R. 423, 116 Fed. 404 (D. C. Ga.): "The decision of the highest court of a State that recording is not essential to the validity of a chattel mortgage executed therein when the state law does not so require, must be followed by the bankruptcy court."

So, where a chattel mortgage was made in a state wherein recording was required and effected, it does not become invalid because the mortgaged property has been removed to a state wherein recording is not required, and cannot be made.⁸²

§ 1232. Meaning of "Required."—And the term "required," as thus used in recording statutes, means not that recording is compulsory nor that it is essential to validity between the immediate parties, but merely that recording is essential to validity as to creditors.⁸³

First Nat'l Bk. *v.* Connett, 15 A. B. R. 662, 142 Fed. 33 (C. C. A. Mo.): "Within the meaning of amended § 60a of the Bankruptcy Act, the Missouri law (Rev. St. 1899, § 3404) required the recording of chattel mortgages. To be sure an unrecorded mortgage is not pronounced void absolutely and under all circumstances, but it 'is required to be recorded' in the sense in which that phrase is customarily used, and the language of requirement is similar to that employed in the registry laws of most of the states. The word 'required,'

constructive notice to creditors. In *re Bazemore*, 26 A. B. R. 494, 189 Fed. 236 (D. C. Ala.).

In *re Geiver*, 28 A. B. R. 413, 193 Fed. 128 (D. C. S. Dak.): "It follows that these chattel mortgages which would have been binding upon, and could have been enforced between the parties hereto, prior to the amendment of the Bankruptcy Law of A. D. 1910, no longer necessarily bind the trustee. His position is no longer the same as that of the bankrupt, but he is now in the position of a creditor holding a legal or equitable lien, and in the case at bar the chattel mortgages are to be interpreted exactly as if the trustee was a creditor holding such lien."

79. *Lindley v. Ross*, 29 A. B. R. 610, 200 Fed. 733 (C. C. A. Ill.).

80. *Millikin v. Second Nat. Bk. of*

Balto., 30 A. B. R. 477, 206 Fed. 14 (C. C. A. Md.), reversing 29 A. B. R. 613, quoted ante, § 1270.

81. Inferentially, *Hewitt v. Berlin Machine Wks.*, 11 A. B. R. 709, 194 U. S. 296. Compare *In re Jacobson & Perrill*, 29 A. B. R. 603, 200 Fed. 812 (D. C. Ga.); *In the Matter of Fred. A. Lausman*, 25 A. B. R. 186, 183 Fed. 647 (D. C. Ky.).

82. *In re Hicks*, 27 A. B. R. 168 (Ref. Tex.).

83. *Loeser v. B'k*, 17 A. B. R. 631, 148 Fed. 975 (C. C. A. Ohio). Contra, and that it refers to validity between the immediate parties, see *Drug Co. v. Drug Co.*, 14 A. B. R. 477, 136 Fed. 396 (C. C. A. Tex.). And see, also, *In re Hunt*, 14 A. B. R. 415, 139 Fed. 283 (D. C. N. Y.). Compare *In re Jacobson & Perrill*, 29 A. B. R. 603, 200 Fed. 812 (D. C. Ga.).

found in the phrase 'the recording or registering of the transfer, if by law such recording or registering is required' of the amendment of § 60a, has reference to the character of the instrument of transfer required to be recorded by the State law rather than to the particular individual who, by reason of adventitious circumstances, may or may not be affected by an unrecorded instrument. Thus an affirmative answer would unhesitatingly be given to the inquiry: 'Does the law of Missouri require the recording of chattel mortgages?'

"The Circuit Court of Appeals of the Fifth Circuit, in a case involving the registry statute of Texas, held that, as an unrecorded chattel mortgage was good between the parties thereto and against ordinary creditors, and as there were no intervening lienholders or purchasers, it could not be said that a registry or recording was required, and upon the facts of that case it accordingly concluded that a chattel mortgage given before but placed on record within the four months before the institution of bankruptcy proceedings could not be considered as a voidable preference. *Meyer Bros. Drug Co. v. Pipkin Drug Co.* (C. C. A.), 14 A. B. R. 477, 136 Fed. 396. In effect this is the adoption, without exception or qualification, of the old rule that whether and to what extent a chattel mortgage given before but recorded within the four months' period is valid against a trustee in bankruptcy should be determined exclusively by the State law. In our opinion, the Amendment of 1903 has qualified this rule in respect of the question whether such a mortgage may constitute a voidable preference under subdivisions 'a' and 'b' of § 60. If this has not resulted, we fail to see that Congress has accomplished anything by the amendment."

And some decisions have held that it means that such recording is essential to validity as to levying creditors;⁸⁴ while other decisions take the broader ground that it means "required" for *any* purpose, whether for validity against levying creditors, "general creditors," "any third person," or merely against innocent purchasers and encumbrancers.⁸⁵

But, at any rate, if the recording is required only to give notice to debtors or to public officers, etc., it is not within the statute, as, for example, where filing of an assignment of a public contract is required to give notice to the disbursing officer.^{85a}

That the transfer is good between the parties without recording does not necessarily remove it from the category of those "required" to be recorded.⁸⁶

§ 1233. Creditor "Armed with Process" No Longer Necessary.

—Before the Amendment of 1910, the doctrine was firmly established, that "creditor" meant levying creditor and that some creditor must have actually levied before bankruptcy, to whose lien the trustee might be subrogated;⁸⁷ but by the Amendment of 1910 to § 47a (2) of the Bankruptcy

⁸⁴. See post, for discussion of entire subject, §§ 1382½, 1383.

⁸⁵. In re Beckhaus, 24 A. B. R. 380, 177 Fed. 141 (C. C. A. Ill.), quoted at § 1383.

^{85a}. In re Interstate Paving Co., 28 A. B. R. 573, 193 Fed. 371 (D. C. N. Y.).

⁸⁶. Ragan v. Donovan, 26 A. B. R.

311, 189 Fed. 138 (D. C. Ohio).

⁸⁷. See discussion, ante, § 1270 note 94.

Thompson v. Fairbanks, 13 A. B. R. 445, 196 U. S. 516; *York Mfg. Co. v. Cassell*, 15 A. B. R. 637, 201 U. S. 344; In re N. Y. Economical Printing Co., 6 A. B. R. 615, 110 Fed. 514 (C. C. A. N. Y.); In re Blake, 17 A. B. R.

Act, the trustee has been endowed with the rights of a creditor "armed with process."⁸⁸

Where the local law does not itself create a lien in favor of even levying creditors on the failure to record a chattel mortgage, the bankruptcy of the mortgagor cannot create such a lien.⁸⁹

§ 1234. Not Void for Simple Nonrecord in States Where Showing of Damage to Creditors or Other Additional Conditions Also Requisite.—A chattel mortgage is not void for nonrecord in States where the simple failure to file or record it is not enough to avoid it unless damage to creditors is shown or the failure was by agreement of parties;⁹⁰ and it is not void for nonrecord in certain other States except as to subsequent creditors without notice, as in Kentucky;⁹¹ nor in Michigan except as to new creditors, or as to old creditors extending additional time between the date of the executing and the date of the filing;⁹² nor in South Carolina for nonrecord except as to creditors becoming such after the execution of the mortgage and before its filing, and such intervening creditors alone may participate in the fund.⁹³ And a similar rule prevails in New Mexico.⁹⁴ In Maryland subsequent creditors or purchasers without notice are not affected by an unrecorded chattel mortgage.⁹⁵ In Georgia an unrecorded chattel mortgage is void only as against lien creditors, or subsequent purchasers and mortgagees or lienholders in good faith.⁹⁶

§ 1235. Not Void in States Where Mere Equitable Sequestrations by Receivers, Assignees, etc., Insufficient.—And is not void where, under State law, mere sequestrations of the property by legal proceedings is insufficient unless accomplished by some particular method of

667 (C. C. A. Mo.); *Hewitt v. Berlin Mach. Wks.*, 11 A. B. R. 709, 194 U. S. 296; *Humphrey v. Tatman*, 14 A. B. R. 75, 198 U. S. 91.

Mistake of Counsel Causing Mortgagee to Relinquish Position as Owner of Goods and to Assume That of Mere Creditor.—In *re Strobel*, 20 A. B. R. 754, 163 Fed. 380 (D. C. N. Y.).

⁸⁸. See ante, § 1137, et seq., and ante, §§ 1207, 1208, 1242 and 1270. Also, see *In re Hammond*, 26 A. B. R. 336, 188 Fed. 1020 (D. C. Ohio).

⁸⁹. *Detroit, etc., Co. v. Pontiac Sav. Bank*, 27 A. B. R. 821, 196 Fed. 29 (C. C. A. Mich.).

⁹⁰. *Holt v. Crucible, etc., Co.*, 27 A. B. R. 856, 224 U. S. 262; *Deland v. Miller*, 11 A. B. R. 744, 93 N. W. Rep. 304, 119 Iowa 368.

⁹¹. In *re Sewell*, 7 A. B. R. 133, 111 Fed. 791 (D. C. Ky.); analogously, In *re Shuster (Ducker)*, 13 A. B. R. 760, 134 Fed. 43 (C. C. A. Ky.); In *re Doran*, 17 A. B. R. 799, 148 Fed. 327

(D. C. Ky.); In *re Doran*, 17 A. B. R. 799, 148 Fed. 327 (D. C. Ky.; modified in 18 A. B. R. 760, 154 Fed. 467). Compare, In *re Doran*, 18 A. B. R. 760, 154 Fed. 467 (C. C. A., modifying 17 A. B. R. 799, 148 Fed. 327).

⁹². In *re Adams*, 2 A. B. R. 415 (Ref. Mich.).

⁹³. Compare, ante, § 1225½. In *re Cannon*, 10 A. B. R. 64, 121 Fed. 582 (S. Car.). *Simmons v. Greer*, 23 A. B. R. 443, 174 Fed. 654 (C. C. A. S. Car.), quoted at § 1225¾. Obiter ("arming with process" also being required), In *re Bailey*, 23 A. B. R. 876, 176 Fed. 628, 176 Fed. 990 (D. C. S. Car.). Compare, analogously, as to conditional sales in Georgia, In *re Braselton*, 22 A. B. R. 419, 169 Fed. 960 (D. C. Ga.).

⁹⁴. In *re Harnden*, 29 A. B. R. 507, 200 Fed. 172 (D. C. New Mex.).

⁹⁵. In *re Riehl*, 29 A. B. R. 613, 200 Fed. 455 (D. C. Md.).

⁹⁶. In *re Jacobson & Perrill*, 29 A. B. R. 603, 200 Fed. 812 (D. C. Ga.).

legal seizure as by levy of execution or attachment.⁹⁷ Probably this distinction lies at the basis of many of the decisions contra to the general rule.⁹⁸

See, inferentially, *In re N. Y. Economical Ptg. Co.*, 6 A. B. R. 619, 110 Fed. 514 (C. C. A. N. Y.): "When the mortgagor was adjudicated bankrupt, there was, so far as appears, but one judgment creditor. Whether any other creditor could have eventually entitled himself to the benefit of the statute was a matter of mere conjecture. It would have depended not only upon his own vigilance in pursuing his legal rights, but also upon the volition of the mortgagor."

§ 1236. Taking of Possession Curing Lack of Record.—But, if possession is taken by the mortgagee or conditional vendor before the bankruptcy petition is filed, such taking of possession operates as a filing and the lien will be good although bankruptcy follows within four months,⁹⁹ unless the mortgage or conditional sale is otherwise void as a preference,¹ or void as containing a power of sale.²

Humphrey v. Tatman, 14 A. B. R. 74, 198 U. S. 91: "In Massachusetts, the taking possession of mortgaged chattels by the mortgagee within the four months period, under an unrecorded mortgage covering after-acquired property, made more than two years before the bankruptcy of the mortgagor, is good as against his trustee." Reversing 12 A. B. R. 62.

§ 1237. Whether Lien Begins at Date of Taking Possession or Reverts, Determined by State Law.—The effect of taking possession as to whether the lien relates back to the date of the original instrument or takes effect as of the date of taking possession is to be determined by State law,³ as interpreted by its highest court.⁴

⁹⁷. See ante, discussion of this subject, division 2 of this chapter.

And in such States the lien of the levy must be preserved by order of court to effect this object. *Thompson v. Fairbanks*, 13 A. B. R. 437, 196 U. S. 516.

⁹⁸. See inferentially, *In re Beede*, 14 A. B. R. 697, 138 Fed. 441 (D. C. N. Y.); *Matthew v. Hardt*, 9 A. B. R. 373 (Sup. Ct. N. Y.); compare, *Skilton v. Codington*, 15 A. B. R. 819, 185 N. Y. 80.

⁹⁹. See post, "Seventh Element of a Preference," § 1371. *In re Antigo Screen Door Co.*, 10 A. B. R. 361, 123 Fed. 249 (C. C. A. Wis.), criticised in *In re Ducker* (*In re Shuster*), 13 A. B. R. 757, 118 Fed. 668 (C. C. A. Ky.); *In re Klingman*, 2 A. B. R. 44 (Ref. Iowa); compare, *Zartman v. Nat'l Bk.*, 16 A. B. R. 158, 106 App. Div. (N. Y.) 406; instance, where facts fail to show possession taken, *In re Shaw*, 17 A. B. R. 204 (D. C. Mo.). Compare, *Hanson v. Blake*, 19 A. B. R. 325, 150 Fed. 342 (D. C. Me.). Compare, *In re Do-*

ran (*Moorman v. Beard*), 18 A. B. R. 760, 154 Fed. 467 (C. C. A. Ky.).

¹. *In re Ball*, 10 A. B. R. 564, 123 Fed. 164 (D. C. Vt.), rejected in *Humphrey v. Tatman*, 14 A. B. R. 74, 198 U. S. 91. Compare, as to similar subject, under "Preferences as Affected by Recording," § 1379. Compare, *In re Reynolds*, 18 A. B. R. 666, 153 Fed. 295 (D. C. Ark.).

². *In re Barker*, 20 A. B. R. 674 (Ref. Colo.); *In re Reynolds*, 18 A. B. R. 666, 153 Fed. 295 (D. C. Ark.); *Zartman v. First Nat. Bank*, 19 A. B. R. 27, 189 N. Y. 267, quoted, on other points, at § 1238, but even power of sale may not vitiate if not applicable to the particular property so taken possession of, *In re Davis*, 19 A. B. R. 98, 153 Fed. 671 (D. C. N. Y.).

³. *In re Newton*, 18 A. B. R. 567, 153 Fed. 841 (C. C. A. Ark.), quoted at §§ 1263, 1381; also, *In re Reynolds*, 18 A. B. R. 666, 153 Fed. 295 (D. C. Ark.).

⁴. See ante, §§ 1140 and 1141; *Thompson v. Fairbanks*, 13 A. B. R. 437, 196 U. S. 516; *Humphrey v. Tatman*, 14 A.

§ 1238. As to After-Acquired Property.—The taking of possession of after-acquired property operates in some States to extend the mortgage lien thereto as of the date of the taking of possession, not as of the date of the original execution of the mortgage, and the same holding will prevail in bankruptcy.⁵

Compare, *Zartman v. First Nat. Bank*, 19 A. B. R. 27, 189 N. Y. 267: "As was said in a case upon which both parties rely: 'The right of the mortgagor in the meantime,' that is, until default, 'to the use of the earnings, amounts, practically, to absolute ownership, and hence the mortgage cannot operate as a lien upon such earnings to the prejudice of the general creditors until actual entry and possession taken, and then only upon what is earned after that time. The lien of the mortgage upon future earnings is consummated as against other creditors only by the fact of the possession of the property, and cannot have any retroactive operation, since it would then deprive the unsecured creditor of the fund, upon the faith of which he may have given credit to the mortgagor during the time when the latter was permitted to deal with and use it as its own. The lien upon the earnings, in favor of the bondholders, attaches only upon what is earned after the time when the lien is perfected by entry and possession.' N. Y. Security & Trust Co. v. Saratoga Gas & El. L. Co., 159 N. Y. 137, 143. If a lien was created by the mortgage upon property not in existence at its date, possession after it came into existence was of no importance. If no lien was created by the mortgage upon such property the taking of possession pursuant to its terms did not create one as against general creditors, who are presumed to have dealt with the mortgagor in reliance upon its absolute ownership of the stock on hand. While the record of the mortgage was notice to all, it was notice of all its terms, which included the right of disposition for the use and benefit of the mortgagor, with no duty to apply the avails upon the mortgage indebtedness. If the question had arisen between the parties to the mortgage, equity might recognize a contract to give a lien and treat it as an actual lien, but it arises between the mortgagee and the general, unsecured creditors, who had little, if anything, to rely upon except the shifting stock, which, directly or indirectly, they themselves had furnished. The credit extended by them enabled the mortgagor to carry on business, and if the product of that credit goes to the mortgagee, not only are they helpless, but, if the law so declared, hereafter manufacturing corporations needing credit will be helpless also."

B. R. 74, 198 U. S. 91; *In re Ball*, 10 A. B. R. 564, 123 Fed. 164 (D. C. Vt.); impliedly, *Zartman v. Nat'l Bk.*, 16 A. B. R. 158, 106 App. Div. 406 (N. Y.). But compare *Christ v. Zehner*, 16 A. B. R. 790, 212 Pa. St. 188, where it is laid down as general law that it is the date of the original execution and delivery of the instrument and not the date of the taking of possession of the goods that governs. Compare, on kindred subject of agreement for liens, post, "Seventh Element of a Preference," § 1373. For discussion of *Thompson v. Fairbanks*, see, among others, *In re Hickerson*, 20 A. B. R. 682, 162 Fed. 345 (D. C. Idaho).

5. *In re Clough*, 28 A. B. R. 828, 197

Fed. 185 (D. C. Vt.); *In re Antigo Screen Door Co.*, 10 A. B. R. 361, 123 Fed. 249 (C. C. A. Wis.); compare, *In re Waterloo Organ Co.*, 9 A. B. R. 427, 118 Fed. 904 (D. C. N. Y.); compare, *Zartman v. Nat'l Bk.*, 16 A. B. R. 158, 106 App. Div. 406 (N. Y.); compare, also, *In re Rogers & Woodward*, 13 A. B. R. 82, 132 Fed. 560 (D. C. Vt.). Compare, facts of *Mattley v. Wolfe*, 23 A. B. R. 673, 175 Fed. 619 (D. C. Neb.), reversed in *Mattley v. Giesler*, 26 A. B. R. 116, 187 Fed. 970 (C. C. A. Neb.). Compare, *In re Medina Quarry Co.*, 24 A. B. R. 769, 179 Fed. 929 (D. C. N. Y.). Compare, on the facts, *In re Flatland*, 28 A. B. R. 476, 196 Fed. 310 (C. C. A. Wash.).

But in other States it operates to fasten the lien as of the date of the original execution of the mortgage, and in such States the lien will likewise be held to revert, in the bankruptcy court.⁶

The identification and separation of chattels within the four months period where they were indefinitely described in the mortgage, itself operates to fix the lien as of the date of the identification.⁷

§ 1239. Permitting Creditor to Levy after Bankruptcy in Order to "Arm with Process."—In some of the States where the rule is adopted that there must be an actual levy by execution or attachment, and that equitable sequestration is not sufficient, the creditors, by some holdings, are permitted to proceed to judgment *after* adjudication of bankruptcy and to levy execution, the levy being held to redound thereupon to the benefit of all creditors.⁸

But it is apparently held in one case that this rule applies only where the suits have been started before bankruptcy.⁹

Perhaps this rule is adopted in analogy to the course suggested in *Lockwood v. Exch. Bk.*, 10 A. B. R. 107, 190 U. S. 294, relative to the right of creditors holding notes waiving exemptions to proceed to judgment notwithstanding the bankruptcy.¹⁰

Amendment of 1910.—The matter is set at rest by the Amendment of 1910 to § 47a (2) whereby the trustee is "deemed to be vested with all the rights, powers and remedies of a creditor armed with process."

§ 1240. Defective Refiling of Chattel Mortgage.—Before the Amendment of 1910, a failure to refile, properly, a chattel mortgage, where under the State law such failure vitiates the mortgage only as to creditors "armed with process," was held, in most states to vitiate it in bankruptcy only where prior to the bankruptcy some creditor had levied execution or attachment, or otherwise was "armed with process."¹¹

And a failure to properly refile a chattel mortgage, after the Amendment of 1910 to § 47a (2) will vitiate the mortgage even though the mortgage

6. *Thompson v. Fairbanks*, 13 A. B. R. 516; *In re Rogers & Woodward*, 13 A. B. R. 82, 132 Fed. 560 (D. C. Vt.). Compare, *In re Ball*, 10 A. B. R. 564 (D. C. Vt.): This case is rejected on this point in *Thompson v. Fairbanks*, 13 A. B. R. 82, 132 Fed. 560 (D. C. Vt.), and *Humphrey v. Tatman*, 14 A. B. R. 74, 198 U. S. 516. Instance, *In re National Valve Co.*, 15 A. B. R. 524, 40 Fed. 679 (D. C. Ohio). Compare, *Hanson v. Blake*, 19 A. B. R. 325, 150 Fed. 342 (D. C. Me.).

Discussion of *Humphrey v. Tatman*.—*Hanson v. Blake*, 19 A. B. R. 325, 150 Fed. 342 (D. C. Me.).

7. *First Nat'l Bk. of Holdredge v. Johnson*, 10 A. B. R. 208, 68 Neb. 641.

8. *In re Beede*, 14 A. B. R. 697, 138 Fed. 441, and 11 A. B. R. 387, 120 Fed. 853 (D. C. N. Y.). But compare, *Gove v. Morton Trust Co.*, 12 A. B. R. 300, 96 N. Y. App. Div. 177.

9. *In re Beede*, 14 A. B. R. 697, 138 Fed. 441 (D. C. N. Y.).

10. See ante, § 1104, et seq.

11. *In re Smith*, 29 A. B. R. 527, 198 Fed. 876 (D. C. Wis.), quoted supra. Before the amendment of 1910 it was held that failure to refile would not vitiate in bankruptcy unless there was a creditor "armed with process." *In re Burnham*, 15 A. B. R. 140 Fed. 926 (D. C. N. Y.); *In re Cutting*, 16 A. B. R. 751, 145 Fed. 388 (D. C. N. Y.).

itself was executed before the amendment, for such holding as to the refileing would not be the same as holding the amendment to be retroactive.

In *re Smith*, 29 A. B. R. 527, 198 Fed. 876 (D. C. Wis.): "It is assumed as well settled that such filing of a renewal affidavit at a time other than that specified in the statute was wholly nugatory, and therefore the two-year limit expired, and the mortgage ceased to be valid as against those designated on September 8th, 1911. Thus, on June 25, 1910, when the amendatory act was passed, the mortgage was effective, not only as between the parties, but as against all others, because it had been filed.

"Can the mortgagee be heard to say that the amendment is inoperative because at the time of the execution and delivery of the mortgage the rights which purchasers, mortgagees, or creditors could assert had not been conferred upon trustees in bankruptcy? As an academic proposition he might plausibly claim that, not being required, as against the trustee, to file the mortgage at all, the immunity against attack by the latter was a valuable right which should remain unimpaired until the mortgage debt is satisfied. But the practical situation is this: He did in fact file the mortgage, and in doing so shielded it against attack from all sources—he secured the full protection which the statute gives to a filed mortgage. He was at liberty to maintain this protection by filing a renewal affidavit, or he could neglect to do so and thereby hazard attack. Has the amendatory act done anything more than in some degree possibly to change the hazard by introducing the trustee into the class or classes permitted by the State statute to question such mortgage if not filed or renewed? At the time the amendment went into effect, did not the situation itself reserve to the mortgagee all of his rights as they then existed; or, to put it in the least favorable light, is not the amendment entirely consistent with his rights under the mortgage if he would but exercise the choice or opportunity given him by the State statute for the preservation thereof? I think this must be answered affirmatively; and, if so, the question respecting the invalidity of the amendment because retroactive, or for any other reason, is wholly eliminated."

But in New York a failure to refile within the thirty days before the expiration of the year renders the mortgage void as against the trustee in bankruptcy,¹² and such was the holding of the later decisions before the Amendment of 1910.¹³

§ 1240¼. Filing or Refiling in Wrong Place.—A failure to file, or to refile, in the proper place, a chattel mortgage or other instrument requiring filing, is in most States the equivalent of no filing; and the consequences of such failure in such States are in bankruptcy the same as no filing.¹⁴

§ 1240½. Or in Only One Place Where Statute Requires Two.—Likewise, a filing in only one place where the statute requires two, as, for instance, in the place of the mortgagor's business but not in that of his residence, where the statute requires both, is fatal; and, in Massachusetts,

12. In *re Watts-Woodward Press, Inc.*, 24 A. B. R. 684, 181 Fed. 71 (C. A. N. Y.).

13. In *re Watts-Woodward Press,*

Inc., 24 A. B. R. 684, 181 Fed. 71 (C. A. N. Y.).

14. In *re McDonald*, 21 A. B. R. 358 (Ref. Mass.), also 23 A. B. R. 51, 173 Fed. 99.

is void as against the trustee, though no creditor "armed with process" exist.¹⁵

§ 1240³. **Defective Execution of Mortgages, etc.**—Whether the defective execution of a mortgage, or other instrument of transfer, where no levy has been made by creditors will render the instrument nugatory as against the trustee, would, on principle, depend on State law, as to whether such defect in execution would render it invalid as to the bankrupt, or as to general creditors.¹⁶

Or, since the Amendment of 1910, as to whether State law would render it invalid as to a creditor "armed with process," the trustee, by that amendment, being deemed so armed.

§ 1241. **Unrecorded or Unfiled Conditional Sales Contracts, Void.**—An unrecorded or unfiled (as the case may be) conditional sale contract is likewise void as against the trustee, in states where recording or filing is required to preserve the vendor's rights as against creditors.¹⁷

15. Instance, *In re McDonald*, 23 A. B. R. 51, 173 Fed. 99 (D. C. Mass.).

16. (Instance, held defect fatal for want of due attestation. *In re Moore*, 19 A. B. R. 271 (Ref. Ga.).

17. *Chesapeake Shoe Co. v. Seldner*, 10 A. B. R. 466, 122 Fed. 598 (C. C. Va.); *In re Sheets Ptg. & Mfg. Co.*, 14 A. B. R. 668 (D. C. Ohio), affirmed sub nom. *Unitype Co. v. Long*, 16 A. B. R. 282 (C. C. A. Ohio); *In re Yukon Wollen Co.*, 2 A. B. R. 805, 96 Fed. 326 (D. C. Conn.); *In re Ducker*, 13 A. B. R. 760, 118 Fed. 668 (C. C. A. Ky.); *McElvan v. Hardesty*, 22 A. B. R. 320, 169 Fed. 32 (C. C. A. Mo.); *In re Fish Bros. Wagon Co.*, 21 A. B. R. 147, 164 Fed. 553 (C. C. A. Kans.), quoted at §§ 1489 and 1603.

In re Faulkner, 25 A. B. R. 416, 181 Fed. 981 (D. C. Conn.); *In re Farmers' Supply Co.*, 28 A. B. R. 535, 196 Fed. 990 (D. C. Ga.); *In re Williamsburg Knitting Mill*, 27 A. B. R. 178, 190 Fed. 871 (D. C. Va.), quoted at § 1270; *In re Nelson*, 27 A. B. R. 272, 191 Fed. 233 (D. C. S. Dak.), quoted at § 1270; *In re Bazemore*, 26 A. B. R. 494, 189 Fed. 236 (D. C. Ala.), quoted at § 1270; *In re Kreuger*, 27 A. B. R. 623, 196 Fed. 705 (D. C. Ky.); *Holt v. Henley*, 27 A. B. R. 578, 196 Fed. 1005 (C. C. A. Va.); *In re Gehris-Herbine*, 26 A. B. R. 470, 188 Fed. 502 (D. C. Pa.); *In re Dancy, etc., Hardware Co.*, 28 A. B. R. 444, 198 Fed. 336 (D. C. Ala.).

In re Tweed, 12 A. B. R. 648, 131 Fed. 355 (D. C. Iowa): "The orders or contracts of March 31st and July 9th, whereby the bankrupt obtained posses-

sion of these carriages, were in effect conditional sales thereof by the carriage company to this bankrupt; and, not having been acknowledged and recorded, the conditions are void, under this section, as against creditors or purchasers from the bankrupt without notice."

Unitype Co. v. Long, 16 A. B. R. 282 (C. C. A. Ohio, affirming *In re Sheets Ptg. & Mfg. Co.*, 14 A. B. R. 668 [D. C. Ohio]). *Bradley, Alderson & Co. v. McAfee*, 17 A. B. R. 495 (D. C. Mo.): Recorded after petition filed but before adjudication. *In re Smith & Shuck*, 13 A. B. R. 103, 132 Fed. 301 (D. C. Iowa); *In re Dunn Hardware Co.*, 13 A. B. R. 147, 134 Fed. 997 (D. C. N. Car.): This was a case of conditional sale disguised as a lease. *In re Press Post Printing Co.*, 13 A. B. R. 797 (D. C. Ohio); *In re Tatem, Mann & Co.*, 6 A. B. R. 426, 110 Fed. 519 (D. C. N. Y.); *In re Hess*, 14 A. B. R. 635, 136 Fed. 988 (Ref. affirmed by D. C. Pa.); *In re Frazier*, 9 A. B. R. 21, 117 Fed. 575 (D. C. Mo.).

In re Gosh, 9 A. B. R. 610, 121 Fed. 604 (D. C. Ga.): Reversed in 12 A. B. R. 149, 126 Fed. 627 (C. C. A. Ga.), but upon the ground that it was recorded in time, being recorded within thirty days of the delivery of the property, that date being construed to be the "date" referred to in the statute, although it was not recorded within thirty days of the approval of the contract.

In re Franklin Lumber Co. (*In re Lumber Co.*), 17 A. B. R. 443, 147 Fed. 852 (D. C. N. J.); *In re Lumber Co.*

§ 1242. Creditors "Armed with Process" No Longer Requisite.—Before the Amendment of 1910 to the Bankruptcy Act, § 47a (2), which endowed the trustee with the attributes of a creditor "armed with process," it was held that unfiled conditional sales contracts were not void as against the trustee unless prior to the bankruptcy some existing creditor had actually levied execution or attachment, or otherwise was "armed with process," legal or equitable, to which the trustee might be subrogated by virtue of § 67 of the Bankruptcy Act;¹⁹ although, of course, if fraud

(Builders' Lumber Co.), 17 A. B. R. 449 (D. C. N. Car.); *In re Galt*, 9 A. B. R. 682 (D. C. Ills., reversed on ground that it was a bailment and not a conditional sale, *In re Galt*, 13 A. B. R. 575, 120 Fed. 64, C. C. A. Ills.); *In re Rabenau*, 9 A. B. R. 180, 118 Fed. 471 (D. C. Mo.); contra, *In re Hinsdale*, 7 A. B. R. 85, 111 Fed. 502 (D. C. Vt.); contra, *In re Kellogg*, 7 A. B. R. 270, 112 Fed. 52 (D. C. N. Y.); instance held properly filed, *In re Franklin*, 18 A. B. R. 218 (D. C. N. Car.). Compare, ante, § 1147½; also compare citations under similar propositions relative to chattel mortgages, ante, § 1230, et seq.

Void Only as to Subsequent Creditors and Lienholders Relying Thereon.—*In re Braselton*, 22 A. B. R. 419, 169 Fed. 960 (D. C. Ga.).

As to invalidity of conditional sales to retailers with power to resell in the ordinary course of trade, see post, § 1263.

Compare *York Mfg. Co. v. Brewster*, 23 A. B. R. 474, 174 Fed. 566 (C. C. A. Tex.), quoted ante, § 1225½, where the court disregards the corporate form of a transfer from the conditional vendee, and holds the conditional sale contract valid as against the transferee from the conditional vendee, though unrecorded.

Recording Part of Instrument.—Failure to record entire contract prevents record of part from operating as constructive notice to creditors. *In re Bazemore*, 26 A. B. R. 494, 189 Fed. 236 (D. C. Ala.).

Amendment of 1910 to Bankr. Act, § 47 (a) (2), Not Retroactive.—It has been held that the Amendment to § 47 (a) (2) giving the trustee the rights of a creditor armed with process is not retroactive so as to divest the rights of the vendor of an unrecorded conditional sales contract executed before that Amendment was enacted. *Arctic Ice Mach. Co. v. Armstrong County Trust Co.*, 27 A. B. R. 562, 192 Fed. 114 (C. C. A. Pa.). But compare, *In re Hammond*, 26 A. B. R. 336, 188 Fed. 1020 (D. C. Ohio), where it is held not to be a retroactive application to ap-

ply it to an instrument executed before the Amendment.

Contra [even though subsequent to Amendment of 1910, on theory that the state law prescribed a rule of "priority" under Bankr. Act § 64 (b) (5)]; *In re Lausman*, 25 A. B. R. 186, 183 Fed. 647 (D. C. Ky.), which, however, is criticised in *In re Williamsburg Knitting Mill*, 27 A. B. R. 187, 188, 190 Fed. 871 (D. C. Va.), wherein the court says: "The only decision since the amended act to which the court's attention has been called is that of *In re Lausman*, * * * This opinion is entitled to much weight by reason of the recognized ability and experience of the judge rendering the same. The case, however, involved a small amount, and it is fair to assume was not presented as fully as has been the case here, and was decided before the publication of the recent editions of Remington and Collier, the former of which called special attention to the reason for the Senate's action, as above indicated."

19. *In re Great Western Mfg. Co.*, 18 A. B. R. 261, 152 Fed. 123 (C. C. A. Neb.); *In re Sewall*, 7 A. B. R. 133, 111 Fed. 791 (D. C. Ky.); obiter, *In re Garcewich*, 8 A. B. R. 149, 115 Fed. 87 (C. C. A. N. Y.); *Davis v. Crompton*, 20 A. B. R. 53, 158 Fed. 735 (C. C. A. Pa.); *In re Dunlop*, 19 A. B. R. 361, 156 Fed. 545 (C. C. A. Minn.); *Am. Mach. Co. v. Norment*, 19 A. B. R. 679, 157 Fed. 801 (C. C. A. N. C.); *In re Bement*, 22 A. B. R. 616, 172 Fed. 98 (C. C. A. Wis.); *Crucible Steel Co. v. Holt*, 23 A. B. R. 302, 174 Fed. 127 (C. C. A. Ky.); *John Deere Plow Co. v. Anderson*, 23 A. B. R. 480, 174 Fed. 815 (C. C. A. Ga.); *In re Cavagnaro*, 16 A. B. R. 320, 143 Fed. 668; instance, *In re Atlanta News Publishing Co.*, 20 A. B. R. 193, 160 Fed. 519; (D. C. Ga.); instance, *In re Fabian*, 18 A. B. R. 488, 151 Fed. 949 (D. C. Pa.); instance, *In re Pierce*, 19 A. B. R. 662, 157 Fed. 755 (C. C. A. N. Dak.); *In re Bailey*, 23 A. B. R. 876, 176 Fed. 628, 176 Fed. 990 (D. C. So. C.). But such unfiled conditional sales contracts were held

existed—for example, if the failure to record the conditional sales contract was brought about through fraud—it was held void in all the states, since, under the prevailing doctrine, the trustee “stood in the bankrupt’s shoes” only in the absence of fraud;²⁰ and the mere sequestration of the property by the bankruptcy court taking possession was held not sufficient “arming with process” to invalidate the unfiled conditional sales contract;²¹ although any prior assignment for the benefit of creditors was held in some states to constitute such an “arming,” the courts holding in such states that the assignment stood in place of a levy for the benefit of all creditors.²²

Amendment of 1910.—However, by the Amendment of 1910 to the Bankruptcy Act, § 47a (2), the trustee has been effectually “armed” with process,²³ so that the trustee is now vested with the rights of judgment creditors, holding a lien on the property in his custody, and an execution returned unsatisfied as to all property not in his custody.²⁴

In *re Calhoun Supply Co.*, 26 A. B. R. 528, 189 Fed. 537 (D. C. Ala.): “The record presents but one question, viz: does the amendment to the Bankruptcy Act of June 25, 1910, extend the rights and remedies of the trustee to those of a judgment creditor under the registration act of Alabama, so as to avoid in favor of the trustee an unrecorded conditional sale.

“Before the amendment to the Bankruptcy Act, the trustee’s title as against a claim under an unrecorded conditional sale, though the State law required record, did not prevail. *Crucible Steel Co. v. Holt* (C. C. A., 6th Cir.), 23 Am. B. R. 302, 174 Fed. 127. It was to obviate this, among other things, that § 47, clause 2, subdivision a, of the act was amended by inserting the words ‘And such trustees, as to all property in the custody or coming into the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon.’ (Statement of Representative Shirley to the House of Representatives, Congressional Record, 61st Congress, 2d session, pages 2552-2554.) And to vest in the trustee the same right to attack secret unrecorded liens, where record was required by the State law, as was given to the judgment creditors and others

to be void even though no creditor “armed with process” existed, in some cases before the Amendment of 1910, as, for example, in *Missouri, Bradley Alderson v. McAfee*, 17 A. B. R. 499 (D. C. Mo.); and obiter, impliedly *McElvain v. Hardesty*, 22 A. B. R. 320, 169 Fed. 31 (C. C. A. Mo.). And also in Georgia, *In re Burke*, 22 A. B. R. 69, 168 Fed. 994 (D. C. Ga.).

²⁰ Instance, *In re Garcewich*, 8 A. B. R. 151, 115 Fed. 87 (C. C. A. N. Y.).

²¹ *York Mfg. Co. v. Cassell*, 15 A. B. R. 633, 201 U. S. 344; *Davis v. Crompton*, 20 A. B. R. 53, 158 Fed. 735 (C. C. A. Pa.); *In re Newton* [Swoford *v. Bryant*], 18 A. B. R. 567, 122 Fed. 103 (C. C. A. Ark.); but contra, *In re Bement* [Smith *v. Mishawaka Woolen Mfg. Co.*], 22 A. B. R. 616, 172 Fed. 98 (C. C. A. Wis.).

²² *In re Fish Brothers Wagon Co.*,

21 A. B. R. 147, 164 Fed. 553 (C. C. A. Kans.).

²³ See discussion, ante, §§ 1137, 1207, 1208, 1227¼, 1270.

²⁴ *In re Farmers’ Supply Co.*, 28 A. B. R. 535, 196 Fed. 990 (D. C. Ga.), quoted at § 1270; *In re Franklin Lumber Co.*, 26 A. B. R. 37, 187 Fed. 281 (D. C. Pa.), quoted at § 1270; *In re Bazemore*, 26 A. B. R. 494, 189 Fed. 236 (D. C. Ala.), quoted at § 1270; *In re Williamsburg Knitt. Mill*, 27 A. B. R. 178, 190 Fed. 871 (D. C. Va.), quoted at § 1270; *In re Kreuger*, 27 A. B. R. 623, 196 Fed. 705 (D. C. Ky.); *In re Nelson*, 27 A. B. R. 272, 191 Fed. 233 (D. C. S. D.), quoted at § 1270; *Holt v. Henley*, 27 A. B. R. 578, 196 Fed. 1005 (C. C. A. Va.); *In re Gehris-Herbine Co.*, 26 A. B. R. 470, 188 Fed. 502 (D. C. Pa.). See ante, § 1137, et seq.; 1207, et seq.

under that law. It seems to me that the language of the amendment should be construed to effectuate this result if it fairly admits of such construction. If the operation of the amendment is restricted to cases in which a creditor has in fact acquired a lien by legal or equitable proceedings, then it adds nothing to the law as it was under the original act. By virtue of § 67 'c' of the original act, the trustee was subrogated to such a lien, if created within four months, and could enforce it for the benefit of the estate. If created beyond four months, from the filing of the petition, it was, of course, valid as against the trustee, under both the original and amended acts. The class of cases, unprovided for by the original act and intended to be reached by the amendment, were those in which no creditors had acquired liens by legal or equitable proceedings and to vest in the trustee for the interest of all creditors the potential rights of creditors with such liens. The language admits of this construction. It recites that such trustee 'shall be deemed vested with all the rights, remedies, and powers of a creditor holding a lien by legal or equitable proceedings thereon.' This language aptly refers to such rights, remedies and powers as a creditor holding such a lien is entitled to under the law, rather than to the rights, remedies and powers of a creditor who had actually fastened a lien on the property of the bankrupt estate. * * * The purpose of Congress was to embrace within these words every class of creditors with liens by legal or equitable proceedings favored by the varying registration laws of each of the States. The registration laws of some States include but one of many classes of such creditors. In that case the purpose of Congress is not to be frustrated as to the included class because other classes included in the amendment were not included also in the registration act of that particular State. The breadth of language was used for the purpose of gathering in all classes protected by all local registration acts, and this purpose would be defeated by the construction contended for by the petitioner."

In re Hartdagen, 26 A. B. R. 532, 189 Fed. 546 (D. C. Pa.): "The claimant is a corporation engaged in manufacturing agricultural implements, having its principal office at Hoosick Falls, N. Y. The bankrupt was a retail dealer in such implements with residence and place of business at Tillie, Adams County, this district. Between September 1900 and January 1910, the claimant entered into four several agreements with the bankrupt and in pursuance of the same delivered to him certain implements consisting of mowers, side delivery rakes, etc. When Hartdagen was adjudged a bankrupt September 13, 1910 some of these implements being in his possession were turned over to the trustee who on demand declined to deliver them to the petitioner and thereafter these proceedings were instituted. * * * The contracts entered into * * * are agreements of sale whereby the title of the property in question passed to James M. Hartdagen, subject to an agreement stated in the contracts to hold the property in question for the benefit of the company, to secure to it the payment of the purchase price of the property so sold. * * *

"This provision of the Bankruptcy Act puts the trustee, in so far as the assets of the estate are concerned, in the position of a lien creditor, and to this extent this case is distinguished from the case of the York Mfg. Co. v. Cassell, and others of its character, which no doubt inspired Congress to enact the amendment recited." This case further quoted at § 1140.

Decisions holding that a trustee has no other rights than such as belonged to the bankrupt are no longer controlling.²⁵

25. In re Gehris-Herbine Co., 26 A. B. R. 470, 188 Fed. 502 (D. C. Pa.).

§ 1243. But Where Filing or Recording Not "Required."—But such conditional sales contracts are not void in states where filing or recording is not necessary as against "creditors."²⁶ And in such states, the Amendment, of course, would not affect these conditional sales contracts, since the trustee is himself a "creditor."

§ 1243¼. Whether Preservation of Lien for Benefit of Estate Requisite.—It would seem, also, that the lien of the levy, as to which the unrecorded instrument is void, should be preserved for the benefit of the estate.²⁷

Davis v. Crompton, 20 A. B. R. 53, 158 Fed. 735 (C. C. A. Pa.): "Now, § 67f further provides that such lien shall be deemed wholly discharged and released 'unless the court shall on due notice order that the right under such levy, judgment, attachment or other lien shall be preserved for the benefit of the estate, and thereupon the same may pass to and shall be preserved by the trustee for the benefit of the estate aforesaid.' The trustee did not attempt to preserve this lien. It was the receiver who, through the restraining order, obtained possession of the property discharged of the lien; no proceedings were then taken to preserve the lien, and it was not until April 4, 1907, in the midst of the controversy arising between the conditional vendor (claimant herein) and the trustee, that the trustee filed a petition praying to be subrogated to the rights of the execution creditor, upon which petition an order of subrogation was entered. An examination of the record shows that the execution creditor no longer had any rights at the time the order of subrogation was made, and therefore, the trustee took nothing by virtue of the said order."

§ 1243½. Whether Extent of Lien Measures Extent of Trustee's Rights.—It would seem to follow, logically, that the extent of such

26. *Hewitt v. Berlin Machine Wks.*, 11 A. B. R. 709, 194 U. S. 296: This was a case arising in New York whose statutes make conditional sales void only as against subsequent purchasers, pledgees or mortgagees in good faith, the Supreme Court holding a trustee in bankruptcy not to be within such terms, the Supreme Court saying: "And the Circuit Court of Appeals adhering to that decision (In re N. Y. Economical Ptg. Co.) held in this case that, inasmuch as by the New York statutes, a conditional sale such as that in question was void only as against subsequent purchasers or pledgees or mortgagees in good faith, the District Court was right, and affirmed the judgment."
* * *

"We concur in this view, which is sustained by decisions under previous bankruptcy laws and is not shaken by a different result in cases arising in States by whose laws conditional sales are void as against creditors."

In re Burkle (apparently), 8 A. B. R.

542, 116 Fed. 766 (D. C. Conn.); In re Dixon (apparently), 12 A. B. R. 191 (Ref. Ga.); In re Bozeman (apparently), 2 A. B. R. 809 (Ref. Ga.); In re Grainger, 20 A. B. R. 166, 160 Fed. 69 (C. C. A. Calif.). Instance, In re Newton & Co. (*Swofford Bros. Dry Goods v. Bryant*), 18 A. B. R. 567, 153 Fed. 841 (C. C. A. Ark., affirmed sub nom. *Bryant v. Swafford*, 22 A. B. R. 111); *Bryant v. Swafford Bros. Co.*, 22 A. B. R. 111, 214 U. S. 279, quoted at § 1141; In re Agnew, 23 A. B. R. 360 (D. C. Miss.), although seller deprived of his rights because of commingling of goods with other goods and because of no accounting of proceeds. *Arctic, etc., Co. v. Armstrong County Trust Co.*, 27 A. B. R. 562, 192 Fed. 114 (C. C. A. Pa.); *Nauman Co. v. Bradshaw*, 27 A. B. R. 565, 193 Fed. 350 (C. C. A. Ia.); In re Lutz, 28 A. B. R. 649, 197 Fed. 492 (D. C. Ark.); In re Forse, 25 A. B. R. 134, 182 Fed. 212 (D. C. N. Y.).

27. See, also, post, § 1491.

creditor's lien would measure the extent of the trustee's rights in the property levied upon as against the conditional vendor; and that as to any excess of the property, over and above the lien, the rights of the conditional vendor would be paramount to those of the trustee precisely as they would be to those of the bankrupt.

In *re* *Economical Printing Co.*, 6 A. B. R. 615, 110 Fed. 514 (C. C. A. N. Y.): "We conclude that, except as to the Reilly judgment, the lien of the mortgage was valid, and that the trustee is entitled only to the amount of that judgment out of the proceeds in the registry of the court."

Unless the same was also void as against the trustee by virtue of his rights under the Amendment of 1910.²⁸

§ 1244. Distinction between Conditional Sales, as Mere Retentions of Title, and Chattel Mortgages, as "Transfers."—The fundamental distinction between conditional sales whereby the seller never parts with title and the buyer never gets title, and chattel mortgages, which are "transfers," must be borne in mind and, if borne in mind, will help to reconcile apparently conflicting decisions as to the effect of failure to record instruments of "transfer."²⁹

Compare, In *re* *Cavagnaro*, 16 A. B. R. 323, 143 Fed. 668 (D. C. N. H.): "The title of the property under the New Hampshire law thus remaining in the vendor, and the right of a particular creditor thus resulting upon principles of estoppel through the creditor's doing something without notice, like that of making an attachment under legal process, it is not influenced much if at all by § 67 of the Bankrupt Act or the decisions thereunder, which in a large sense relate to situations where the debtor has undertaken to place liens upon property, the title to which was in himself rather than in a vendor."

§ 1245. Critical Analysis of State Statutes Requisite to Reconcile Decisions.—And a critical analysis of the State statutes is requisite to reconcile the apparently conflicting decisions.³⁰

²⁸. See post, § 1491½.

²⁹. Compare post, §§ 1334¾ and 1372½. Compare, also, *Mishawaka Woolen Mfg. Co. v. Smith*, 20 A. B. R. 317, 158 Fed. 885 (D. C. Wis.); also, In *re* *Dunlop*, 19 A. B. R. 361, 156 Fed. 545 (C. C. A. Minn.); also, *Am. Mach. Co.*, 19 A. B. R. 679, 157 Fed. 801 (C. C. A. N. Car.); also compare, suggestively, In *re* *Milbourne Mills Co.*, 20 A. B. R. 746, 162 Fed. 988 (D. C. Pa., affirmed sub nom. *Fourth St. Nat. Bk. v. Millborne Mills Co.*, 22 A. B. R. 442, 172 Fed. 177 (C. C. A.)).

³⁰. **Power of Sale in Conditional Vendee.**—But even in States where actual levy is thus required to invalidate the lien for mere nonrecording, if the vendee is given the right to sell in the ordinary course of trade it would seem the property passes to the trustee in

bankruptcy regardless of levy or lack of levy. See next subdivision, post, § 1263.

In *re* *Garcewich*, 8 A. B. R. 151, 115 Fed. 87 (C. C. A. N. Y.): "When the property is delivered to the vendee for consumption or sale, or to be dealt with in any way inconsistent with the ownership of the seller, or so as to destroy his lien or right of property, the transaction cannot be upheld as a conditional sale, and is a fraud upon the creditors of the vendee. Even in the case of a chattel mortgage, when it is understood between the mortgagor and the mortgagee, that the mortgagor may sell the chattels in his business, and use the proceeds, the transaction is fraudulent in law as against the creditors of the mortgagor. Such an arrangement, if expressed in

In *re Cavagnaro*, 16 A. B. R. 322, 143 Fed. 668 (D. C. N. H.): "Much of the apparent conflict upon the authorities, in respect to the title of a trustee in bankruptcy to property in possession of the bankrupt under conditional sales, is relieved by a critical examination of the particular phraseology of the statutes upon which the various decisions are founded. In some of the States it is declared by statute that unrecorded conditional sales are only good as between the vendor and vendee, while in others that they shall be void for want of record as against creditors, subsequent purchasers, pledgees, or mortgagees, and in others that the contract shall be recorded within thirty days of the delivery of the property, and in others that it shall be acknowledged and recorded in order to be binding as against others than the vendee and his heirs. *Isaac on Conditional Sales in Bankruptcy*, 9-12. Thus, it will be seen, under some of the State statutes creditors may hold against an unrecorded conditional contract of sale without regard to the question of actual notice, and under such circumstances trustees in bankruptcy reasonably enough hold a status, with respect to the title of the property, different from that which would exist under a State statute, where the property could only be held under judicial process by an attaching creditor without notice. Hence, it becomes essential to look at the particular provisions of the New Hampshire statute and the New Hampshire authorities as to the status of the title under a conditional sale like the one in question."

§ 1246. Disguised Conditional Sales, Void for Want of Record.—Transfers amounting to conditional sales, unfiled but pretended to be consignments, leases or conveyances of other interests not requiring filing or recording—the property passes.³¹

§ 1246½. Bills of Sale as Mortgages.—Bills of sale given as security are mortgages, and follow the same rules with regard to filing, powers of sale, etc., as mortgages.³²

In *re Reynolds*, 18 A. B. R. 666, 153 Fed. 295 (D. C. Ark.): "It is conceded

the instrument, defeats its essential nature and qualities as a mortgage, so that, in a legal sense, it is not a security, but merely the expression of a confidence, by the mortgagee in the mortgagor; and, if made, but not expressed in the instrument, is equally vicious, if not more suggestive of fraudulent purpose."

In Pennsylvania conditional sales are void as to creditors (whether recorded or not). In *re Butterwick*, 12 A. B. R. 536, 131 Fed. 371 (D. C. Penn.).

In some States, conditional sales contracts are not void for nonrecord except as to subsequent creditors without notice. And the burden of proof rests on such creditors. In *re Sewell*, 7 A. B. R. 133, 111 Fed. 791 (D. C. Ky.).

Apparently some such qualification appears to be the law in Georgia. In *re Dixon*, 13 A. B. R. 191 (Ref. Ga.).

In *re Burk*, 22 A. B. R. 69, 168 Fed. 994 (D. C. Ga.), quoted at § 1141; instance, In *re Agnew*, 23 A. B. R. 360

(D. C. Miss.); instance, In *re Atlanta News Pub. Co.*, 20 A. B. R. 193, 160 Fed. 519 (D. C. Ga.); instance, In *re Barker*, 20 A. B. R. 674 (Ref. Colo.); instance, In *re Newton*, 18 A. B. R. 567, 153 Fed. 841 (C. C. A. Ark.); instance, In *re Reynolds*, 18 A. B. R. 666, 153 Fed. 295 (D. C. Ark.); instance, *Zartman v. First Nat. Bank*, 19 A. B. R. 27, 189 N. Y. 267; instance, In *re Pierce*, 19 A. B. R. 662, 157 Fed. 755 (C. C. A. N. Dak.); impliedly, *First Nat. Bk. v. Guarantee Title & Trust Co.*, 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.).

³¹. See ante, subdivision "B," this division and chapter, § 1228.

In *re Hartdagen*, 26 A. B. R. 532, 189 Fed. 546 (D. C. Pa.), quoted at §§ 1140 and 1242; In *re Franklin Lumber Co.*, 26 A. B. R. 37, 187 Fed. 281 (D. C. Pa.), quoted at § 1270.

³². Impliedly, In *re Gerstman & Bandman*, 19 A. B. R. 147, 157 Fed. 549 (C. C. A. N. Y.).

that the bill of sale was, in fact, a mortgage, and under the decisions of the Supreme Court of Arkansas that concession is correct."

Compare, instance, *Low v. Taylor*, 19 A. B. R. 879, 68 Atl. (N. J.) 128: "Where a bill of sale was given, unaccompanied by the delivery of possession of the property to the vendee and it was shown to have been made merely as security for money loaned and goods purchased, and was not executed and recorded as required by the chattel mortgage act, it will be set aside and declared void as against creditors represented by a trustee in bankruptcy of the party executing the same."

§ 1247. Chattel Mortgages or Conditional Sales Made in State Where Recording Not Required but Contemplating Delivery Where Required and Vice Versa.—A chattel mortgage³³ or a conditional sale contract³⁴ made in a State whose laws do not require the filing or recording of such mortgages or contracts, which contemplates delivery or use in another State whose laws do require such filing, is governed by the laws of the latter state, and if the chattel mortgage or conditional sale contract is not filed or recorded, and the purchaser goes into bankruptcy, then the trustee of the bankrupt purchaser takes the property free from the liens.

On the other hand, where such an instrument is made in one State, the statutes of which provide for recording in the county "wherein the property shall be kept," and the property covered by said contract is to be kept at a place in another jurisdiction, the statutes of which provide that where a conditional sale made in one State contemplates or expressly provides that the property is to be delivered or used in another State the law of the latter State governs, and if no law of that State inhibits contracts of conditional sale, the validity of the contract in question is to be tested under the general law upon the subject.³⁵

§ 1247½. Removing Mortgaged Chattels or Chattels Sold under Conditional Sale to Another State, without Consent.—Where mortgaged chattels or chattels sold under conditional sale are removed from the state where the mortgage or conditional sales contract has been duly recorded, without the mortgagee's or conditional vendor's consent, the lien of the mortgagee and the rights of the conditional vendor remain unaffected.

§ 1248. Unrecorded Real Estate Mortgages.—Unrecorded real estate mortgages are also void as against the trustee where the State statutes or decisions declare them void as against creditors;³⁶ but are not void

³³. In re Greene, 13 A. B. R. 504, 134 Fed. 137 (D. C. Conn.).

³⁴. In re Yukon Woolen Co., 2 A. B. R. 805, 96 Fed. 326 (D. C. Conn., citing *Hart v. Mfg. Co.*, 7 Fed. 543; *Pitts. Loco. & Car Wks. v. State Nat'l Bk. of Keokuk*, Fed. Cas., No. 11,198; *Heryford v. Davis*, 102 U. S. 235; *Chic. Ry. Eq. Co. v. Merchants' Bk.*, 136 U. S. 280). Compare impliedly, In re Gehris-

Herbine Co., 26 A. B. R. 470, 188 Fed. 502 (D. C. Pa.).

³⁵. In re Gray, 21 A. B. R. 375, 170 Fed. 638 (D. C. Okla.).

³⁶. *Rosenbluth v. DeForest, etc., Co.*, 27 A. B. R. 359 (Sup. Ct. Conn.); In re Buchner, 29 A. B. R. 179, 502 Fed. 979 (D. C. Ill.); In re Lukens, 14 A. B. R. 683, 138 Fed. 188 (D. C. Pa.), although it does not appear in this case

where the State law declares them good against creditors.³⁷

The Amendment of 1910, § 47a (2), endowing the trustee with the rights of a creditor "armed with process," is applicable to real estate.³⁸

Sturdivant Bank v. Schade, 27 A. B. R. 673, 195 Fed. 188 (C. C. A. Mo.) (Reversing *In re Jackson Brick & Tile Co.*, 26 A. B. R. 916); "The trustee being in possession of the real estate upon which the lien is claimed by virtue of § 47a of the Bankruptcy Act, must be deemed a creditor holding a lien thereon by legal or equitable proceeding." In this case, however, the court held the mortgage valid because good against levying creditor under state law.

An unwitnessed though otherwise duly executed real estate mortgage has been held not to be a lien in Ohio but to be only a contract to give a lien upon which action for specific performance must be begun before the bankruptcy of the mortgagor else it will be invalid as to the trustee in bankruptcy, such holding even having been made in a case arising before the Amendment of 1910 giving the trustee the right of a levying creditor, the court declaring that the principles of *Cassell v. York* did not apply to real estate mortgages and doubting whether the Supreme Court rightly apprehended the Ohio law in the *Cassell v. York* case, at best.³⁹

So, in some jurisdictions, an assignment of a mortgage must be recorded in order that it may be valid as against the trustee in bankruptcy.⁴⁰

§ 1249. Unrecorded Sales of Personalty Where Property Still in Seller's Hands.—Unrecorded sales of personalty where the property remains in the hands of the seller are void in some states.⁴¹

§ 1250. Other Liens and Contracts Not Requiring Record.—Where the statute does not require filing a lien is good without it.⁴²

Thus, it has been held that the assignment of a contract, under the New York Lien Law, need not be recorded in order to be effective as against the contractor's trustee in bankruptcy, because that law does not render such an assignment void as to general creditors or creditors entitled to file

whether the State statute required real estate mortgages to be recorded in order to be valid against creditors. In *re Noel*, 14 A. B. R. 715, 137 Fed. 694 (D. C. Md.).

In *re Thorp*, 12 A. B. R. 195 (Ref. Va., affirmed by D. C.): An instance of an unrecorded "deed of trust" in Virginia. But this case is wrongly based on the theory that the trustee is an "innocent purchaser."

37. In *re McIntosh*, 18 A. B. R. 173 (C. C. A. Calif.): In California, New York and many other states unrecorded real estate mortgages are good even against levying creditors. In *re Hunt*, 14 A. B. R. 416, 139 Fed. 283 (D. C. N. Y.); *obiter*, *Butcher v. Werksman*, 30 A. B. R. 332, 204 Fed. 330 (D. C. N. Y.).

38. *Sturdivant Bank v. Schade*, 27 A. B. R. 673, 195 Fed. 188 (C. C. A. Mo.), reversing *In re Jackson Brick & Tile Co.*, 26 A. B. R. 916.

Compare *In re Snelling*, 29 A. B. R. 818, 202 Fed. 259 (D. C. Mass.), where it was held that real estate in the hands of a third party holding under claim of right thereto was not affected by the Amendment of 1910.

39. *Foerstner v. Citizens Sav. & Trust Co.*, 26 A. B. R. 377, 186 Fed. 1 (C. C. A. Ohio).

40. In *re Buchner*, 29 A. B. R. 179, 207 Fed. 979 (D. C. Ill.).

41. In *re Tweed*, 12 A. B. R. 648, 131 Fed. 355 (D. C. Iowa).

42. See ante, § 1143 division 1 of this chapter, "Trustee's Title, as Successor to Bankrupt." See also, §§ 1231, 1243.

liens for failure to record it.⁴³

§ 1251. Owner's Lien on Material Left on Premises by Bankrupt Contractor.—Thus, the owner's lien upon material left on the premises by a bankrupt contractor, which by contract the owner is entitled to use in completing the job, is not void, although the contract is not recorded.⁴⁴

§ 1252. Equitable Liens upon Property Already Pledged and in Pledgee's Hands.—Likewise, a pledge without delivery of the article involved, may be made operative as an equitable lien, where definite enough, and will be good without recording if the Statute does not require recording.⁴⁵

§ 1253. Agreement to Insure Operating as Equitable Assignment.—Likewise an agreement, made at the time of the passing of the consideration, to procure and assign fire insurance policies on the goods to be purchased with the consideration, will operate as an equitable assignment and be valid in bankruptcy.⁴⁶

Similarly an oral agreement to procure fire insurance for the benefit of a mortgagee will operate as an equitable assignment of the proceeds of policies taken out in the mortgagor's own name,⁴⁷ but not of policies taken out by the grantee of the equity of redemption.⁴⁸

§ 1253½. Other Equitable Liens and Assignments and Powers of Sale Not Requiring Record.—Other equitable liens and equitable assignments, where valid by State law without record, have been held valid in bankruptcy.

But the essentials of an equitable lien must exist.⁴⁹

Fourth St. Nat. Bank *v.* Millbourne Mills Co., 22 A. B. R. 442, 172 Fed. 177 (C. C. A. Pa.): "It is, however, contended that, there being an intent to pledge, an equitable lien was at least created, which entitles the certificate holders to the fund. It is difficult to see, how a transaction, which, for want of delivery, is ineffective as a pledge, can be pieced out, so as to make it hold as something

43. *In re Interstate Pav. Co.*, 28 A. B. R. 573, 197 Fed. 371 (D. C. N. Y.).

44. *Duplan Silk Co. v. Spencer*, 8 A. B. R. 367, 115 Fed. 689 (C. C. A. Penn., reversing *Spencer v. Duplan Silk Co.*, 7 A. B. R. 564, 112 Fed. 638).

45. *Bank v. Rome Iron Co.*, 4 A. B. R. 441, 102 Fed. 755 (C. C. A. Ga.); compare, *Ryttenberg v. Shefer*, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.): In this case the court held the facts did not make out a case of equitable lien. *In re Francis J. Bird*, 25 A. B. R. 24, 180 Fed. 229 (D. C. Minn.).

46. See cases cited post, under "Voidable Preferences," "Seventh Element of a Preference," § 1370, et seq. Also, see ante, § 1150.

47. *Hanson v. Blake*, 19 A. B. R. 325, 150 Fed. 340 (D. C. Me.).

48. *Hanson v. Blake*, 19 A. B. R. 325, 150 Fed. 340 (D. C. Me.).

49. Compare ante, § 1150, where bankrupt's title taken in absence of fraud and of any levying creditor; and ante, § 1222½, where void for fraud. Compare post, § 1372; compare, *In re Southern Textile Co.*, 23 A. B. R. 170, 174 Fed. 523 (C. C. N. Y.), wherein it was held to be simply a disguised chattel mortgage.

And it was held that a receipt to an auctioneer for advances to the owner and for expenses did not constitute an equitable assignment on the proceeds

else. There would be little left to the established doctrine with regard to pledges, if that was the case; and it is somewhat singular, that in all the litigation, where pledges of personal property have been upset, for want of a delivery, no one should have discovered this easy way out. This is not to say, that an equitable lien, under some circumstances, may not exist; but only that there is nothing to support it here. It never arises or is enforced except against property in the hands of a party to the original transaction out of which it is claimed to grow, or his voluntary representatives, or one who has notice of it and is affected with it as a superior right; within which all the cases cited in support of it will be found to fall. 19 Am. & Eng. Encys. (2 Ed.) 36. It is not good as against a trustee in bankruptcy, taking title, in the interest of creditors, by operation of law, as is the case here."

Thus, where a vendor's lien is claimed the essentials of a vendor's lien must exist.⁵⁰

§ 1254. But Liens Absolutely Void, Void Also in Bankruptcy.—If the lien is void in any event, as conditional sales in Pennsylvania, which are void as to creditors, it is void in bankruptcy.⁵²

§ 1255. Mechanics' and Subcontractors' Liens Not Filed Till after Bankruptcy.—Mechanics' and subcontractors' liens are not void for want of filing or recording before bankruptcy, if they are filed afterwards within the statutory time from the furnishing of the work or materials; because such liens are not void as to levying creditors under State law.⁵³

§ 1256. Recording, Where Lien on Both Real and Personal Property.—Instruments recorded properly as chattel mortgages, but not as real estate mortgages, will not operate as liens upon buildings belonging to lessees and removable by them where leaseholds are regarded as real estate.⁵⁴

§ 1257. Liens Invalid under State Law for Other Reasons than Lack of Record, Void.—Claims which for any other reason than for want of record would not have been valid liens against the claims of any creditor of the bankrupt also are not liens against his estate.⁵⁵

of the property, where the auction sale was interrupted and the actual sale was made months afterward by the trustee in bankruptcy. *In re Faulhaber Stable Co.*, 22 A. B. R. 381, 170 Fed. 68 (C. C. A. N. Y.).

50. *In re Teter*, 23 A. B. R. 223, 173 Fed. 798 (D. C. W. Va.).

52. *In re Butterwick*, 12 A. B. R. 536, 131 Fed. 371 (D. C. Penn.).

53. See ante, division 1 of this chapter, subdivision "B," "Mechanics' and Subcontractors' Liens," § 1154, et seq.

54. *In re Rogers & Woodward*, 13 A. B. R. 82, 132 Fed. 560 (D. C. Vt.). Compare, *In re Reynolds*, 18 A. B. R. 666, 153 Fed. 295 (D. C. Ark.).

55. Bankr. Act, § 67 (a). See "Fraudulent Transfers and Property Held on Secret Trust," ante, div. 2, subdiv. "A," § 1209, et seq. Chattel mortgages not valid as against creditors unless on certain specified articles named in statute, but good between parties on others, good as against the trustee as to both, where no previous levy made, *In re Grainger*, 20 A. B. R. 166, 160 Fed. 69 (C. C. A. Calif.). But compare effect of Amendment of 1910, post, § 1270.

This section of the statute is referred to in *Mattley v. Wolfe*, 23 A. B. R. 673, 175 Fed. 619 (D. C. Neb.), reversed in *Mattley v. Giesler*, 26 A.

§ 1258. Chattel Mortgages with Power of Sale, When Void.—

Chattel mortgages with power of sale are void as against the trustee if there is no agreement that the proceeds be applied on the debt, where such mortgages are held void as to creditors by the law of the state.⁵⁶

The goods which the chattel mortgage thus authorizes the bankrupt to sell must pass to the trustee under § 70 as being property which the bankrupt might have transferred before the bankruptcy.

Skillen v. Endelman, 11 A. B. R. 768, 79 N. Y. Supp. 413: "Where there is an agreement or understanding between the parties, at the time of the execution of a chattel mortgage, that the mortgagor may sell or dispose of the mortgaged property, or any portion thereof, for his own use, the mortgage is void as to the creditors of the mortgagor, and this agreement or understanding may be proved by parol, or may be inferred from the fact that the mortgagee permits the sale to be made."

B. R. 116, 187 Fed. 970 (C. C. A. Nev.), quoted at §§ 1379, 1382½, 1383.

Rights of surviving partner and creditors, where partnership had pledged and assigned future accounts but surviving partner had created new accounts. *Natl. Bank v. Title & Trust Co.*, 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.).

⁵⁶. In re Hull, 8 A. B. R. 302, 115 Fed. 858 (D. C. Vt.); In re Tucker, 20 A. B. R. 404, 161 Fed. 584 (D. C. N. Car.); *Knapp v. Milw. Trust Co.*, 20 A. B. R. 671, 162 Fed. 675 (C. C. A. Wis., affirming In re Standard Tel. Co., 19 A. B. R. 491, 157 Fed. 106); In re Barker, 20 A. B. R. 674 (Ref. Colo.); In re Hickerson, 20 A. B. R. 682, 162 Fed. 345 (D. C. Idaho); In re Davis, 19 A. B. R. 98, 155 Fed. 671 (D. C. N. Y.); impliedly, In re Bellevue Pipe & Fdy. Co., 22 A. B. R. 97, 16 Ohio Dec. 247 (Ref. Ohio); *Mitchell v. Mitchell*, 17 A. B. R. 389, 147 Fed. 280 (D. C. N. Car.), affirmed in In re Tucker, 20 A. B. R. 404; In re Noethen, 27 A. B. R. 910, 195 Fed. 573 (D. C. N. Y.); In re Volence, 27 A. B. R. 914, 197 Fed. 232 (D. C. N. Y.); In re Hammond, 26 A. B. R. 336, 188 Fed. 1020 (D. C. Ohio), quoted at § 1270; In re Geiver, 28 A. B. R. 413, 193 Fed. 128 (D. C. S. Dak.); obiter, In re Hartman, 26 A. B. R. 76, 185 Fed. 196 (D. C. N. Y.); compare, obiter, In re Mahland, 26 A. B. R. 81, 184 Fed. 743 (D. C. N. Y.). See analogous doctrine as to conditional sales, ante, preceding subdivisions of this division. *Dodge v. Norlin*, 13 A. B. R. 176, 133 Fed. 363 (C. C. A. Colo.); In re Dry Dock Co., 16 A. B. R. 325 (C. C. A. N. Y.), modifying In re Marine Construction & Dry Dock Co., 14 A. B. R. 466 (D. C. N. Y.); In re Ditsch, 17 A. B. R. 912 (D. C. Kas.); obiter, In re

Burnham, 15 A. B. R. 552 (D. C. N. Y.); compare, to same effect, in State Court in actions wherein the trustee is interested, *Skilton v. Codington*, 15 A. B. R. 820, 185 N. Y. 80; to same effect, *Zartman v. Nat'l Bk.*, 16 A. B. R. 155, 106 App. Div. (N. Y.) 406; compare, to same effect: *Mitchell v. Mitchell*, 17 A. B. R. 389 (D. C. N. Car.). Compare, In re Jules & Frederic Co., 27 A. B. R. 136, 193 Fed. 533 (D. C. Mass.), where the court held an attempted delivery of a stock in trade under a chattel mortgage to be insufficient.

One case has held them void even where held not void by State tribunals, the U. S. Supreme Court having held them void as a rule of general law. In re Hull, 8 A. B. R. 302, 115 Fed. 858 (D. C. Vt.). But see now, *Thompson v. Fairbanks*, 196 U. S. 516, 13 A. B. R. 437. Also, see In re Nat'l Bk., 14 A. B. R. 180, 135 Fed. 62 (C. C. A. Ohio).

Chattel mortgages with power of sale, where the proceeds of the sales are not applied on the debt, are void as to creditors under § 67 (e). In re Egan State Bk. v. Rice, 9 A. B. R. 437, 119 Fed. 107 (C. C. A. S. Dak., affirming In re Platts, 6 A. B. R. 568). See post, division 3 of this chapter, subdivision "C."

Facts held not to constitute chattel mortgage: Executory sale of bankrupt's entire season's output of lumber; lumber left on seller's premises and merely tagged with buyer's name; and permission given to seller to retail therefrom provided replacement be made; considerable more advanced on total purchase price than lumber up to that time manufactured; security taken for excess; held entire transaction does not amount to mortgage. *Stelling v. G. W. Jones Lumber Co.*, 8 A. B. R. 521, 116 Fed. 261 (C. C. A. Wis.).

In *re National Bank of Canton*, 14 A. B. R. 180, 135 Fed. 62 (C. C. A. Ohio): "Under the settled law of Ohio, the question of good faith is not vital if, under a mortgage of a stock of merchandise, it is expressly or impliedly, provided that the mortgagor shall remain in business as before until condition broken or the mortgagee in his own interest chooses to dispossess him.

"If the instrument has in fact been made in good faith it becomes an effectual security notwithstanding such a provision, from the time the mortgagee takes actual possession.

"But before possession taken such an instrument is void as matter of law as to purchasers and creditors of the mortgagor. * * *

"It is also noticeable that the mortgage contains no clause requiring the mortgagor to account for sales nor that the lien should extend to goods afterwards purchased. * * *

"But with reference to the effect of a mortgage upon a stock of goods with the right of the mortgagor to remain in possession and continue business, the instrument is fraudulent in law regardless of registration, and void as to creditors who acquire rights before the mortgagee takes actual possession. Here the mortgagee never took possession and the seizure under the bankruptcy proceedings, therefore, occurred before the mortgage was validated."

Zartman v. First Nat. Bank, 19 A. B. R. 27, 189 N. Y. 267: "* * * because an agreement permitting the mortgagor to sell for his own benefit renders the mortgage fraudulent as matter of law as to the creditors represented by the plaintiff."

In *re Construction & Dry Dock Co.*, 14 A. B. R. 466 (D. C. N. Y., modified, 16 A. B. R. 325): "As already stated, in the *Roberts* case, the mortgagor sold, and was permitted to sell, goods in a store; in the *Benner* case he was empowered to sell lumber; in the case at bar it was contemplated that it should sell material and ships, and it was free to use and consume its stock of materials on hand for the purposes of its business. A mortgage on a pound of sugar and one on a ship should be alike invalid where the same power of disposition is given to the mortgagor. The money was loaned for the very essential purpose of vitalizing the business, so that its stock and material might be made into ships, or other structures to be sold and repaired. Assume that money is loaned to a baker to enable him to conduct his business and to secure the loan a mortgage is taken on the flour constituting the baker's stock in trade, and he is empowered to convert such flour into loaves of bread and to sell the same, would any one contend that the mortgage was an effectual lien upon either the flour or the loaves? In such case the parties constitute the material, and whatever results therefrom, articles of commerce, and the manifest intention is that they shall be sold free from the mortgage. In principle, there is no difference between material in a shipyard, authorized to be converted into boats and ships, and thereupon sold, and flour which is authorized by the parties to be converted into loaves of bread and sold. The magnitude or qualities of the article, or the structure into which it is intended that they shall enter, should not mislead the reason. The law has a common application. If articles are left with the mortgagor to sell in the course of his business and for the purposes of his business, then, under the decisions considered, the mortgage is invalid. If a rule exists, it should be applied logically."

In *re Standard Tel. Co.*, 19 A. B. R. 491, 157 Fed. 106 (D. C. Wis.), affirmed sub. nom. *Knapp v. Milw. Tr. Co.*, 20 A. B. R. 671, 162 Fed. 675 (C. C. A.): "The question of law arising in this case involves the construction of a Wisconsin statute. It is therefore a local question, as the federal court in such a case adopts

the ruling of the highest judicial tribunal of the State. This proposition is so familiar as to require the citation of no authorities. The Wisconsin Supreme Court has consistently held that a chattel mortgage, which upon its face stipulates that the mortgagor may retain possession of the mortgaged property, sell and dispose of the same in the usual course of business, and appropriate any part of such proceeds to his own use and benefit, is fraudulent and void as to creditors. * * * Under these cases it is not a question of intent, because such an arrangement necessarily tends to hinder, delay, and defraud creditors. The mischief that called forth this stringent doctrine was the hardship imposed upon the general creditor who found between him and his debtor a chattel mortgage on a stock of goods which allowed the mortgagor to retain possession, and to appropriate to his own use, the avails of the business, while such creditor was remediless. As against such creditor, such a mortgagor under Wisconsin decisions is void as matter of law without regard to the question of the intention of the parties to the mortgage. The mortgage in suit expressly allows the mortgagor the privilege of disposing of the avails of the business to its own uses and purposes, provided only: (a) The interest on the bond is paid; (b) the sinking fund, amounting to \$500 per quarter, or \$2,000 per annum, is provided for. Beyond this the power of sale and appropriation is unrestrained. But the mortgage under consideration contains another more obnoxious provision. By express terms it is stipulated that if and when the mortgagee shall consent to waive the requirements as to the sinking fund, then and in that case the mortgagor is simply required to keep up the interest on the bonds, and is at liberty to apply all the balance of the proceeds of the business to its own uses and purposes. Thus a secret agreement between the parties may result in continuing the lien of the mortgagee indefinitely, and furnish a cover to protect the mortgagor from attacks of creditors while using the proceeds of the business as though the same were his own."

In *re Standard Tel. & Elec. Co.* (*Knapp v. Milw. Tr. Co.*), 24 A. B. R. 761, 216 U. S. 545 (affirming 20 A. B. R. 671, 162 Fed. 675, C. C. A., and 19 A. B. R. 491, 157 Fed. 106, D. C.): "It was found as a matter of fact that no statement was filed of the amount of the sales, amount of new stock bought, amount applied on mortgage, etc., every sixty days, as required by the Wisconsin statute, § 2316b; that since the execution of the mortgage the company, in the course of its business, made sales from the mortgaged property and applied the proceeds to its own use; that the property was in possession of the mortgagor; that Knapp, the trustee, knew that the business was being so transacted; that it was understood that the business should be so transacted and sales of the mortgaged property so applied to the mortgagor's use.

"While there was a finding that no intentional bad faith was shown, still we agree with the Court of Appeals and the district judge that, under the law of Wisconsin, as construed by her highest court, such conditions as were contained in these mortgages rendered them fraudulent in law and void as to creditors." Quotation from this decision is continued at § 1211. It is also quoted on questions of procedure at §§ 2875 and 2969.

And this is equally true as to a contract which, in effect, operates as a chattel mortgage.⁵⁷

And it is void, even where the mortgagee has actually seized the goods before bankruptcy, in some states.⁵⁸

⁵⁷ In *re Marengo, etc., Co.*, 29 A. B. R. 46, 199 Fed. 474 (D. C. Ala.).

⁵⁸ In *re Barker*, 20 A. B. R. 674 (Ref. Colo.).

In *re Reynolds*, 18 A. B. R. 666, 153 Fed. 295 (D. C. Ark.): "These decisions strike down the mortgage in controversy, in so far as it applies to chattels left in the hands of the bankrupt with the right to sell in the usual course of business. The mortgage on the stock of merchandise left in the possession of the bankrupt with the right to sell in the usual course of business, and to buy and add new stock in the same manner, was void as to creditors *ab initio*, and continued void even after the possession was taken, for the reason that it was a fraud upon creditors under the Arkansas decisions."

And is void whether the mortgage is recorded or not.⁵⁹

In some states, however, the objectionable feature of such mortgages is eliminated by taking possession of the property, pursuant to a reserved power, before a creditor asserts a right thereto by seizure or otherwise.⁶⁰

And such mortgages are valid in some jurisdictions.^{60a}

§ 1259. Not Void if Agreement to Apply Exists Though Agreement Disregarded.—But such mortgage is not void where there is an agreement that the mortgagor should so apply the proceeds.⁶¹

And this is so even though the obligation is disregarded by the mortgagor, if without the mortgagee's consent.⁶²

But if the mortgagee consents, or knowingly acquiesces, the chattel mortgage is void.

In *re Hartman*, 26 A. B. R. 76, 185 Fed. 196 (D. C. N. Y.): "But when it appears that what was done was in pursuance of a common understanding and with the knowledge and concurrence of both the mortgagor and mortgagee, the conclusion is irresistible that the parties acted pursuant to the agreement actually made, whatever may be found expressed in the mortgage itself."

And in some states, even before the Amendment of 1910 giving the trustee the right of a levying creditor, the mortgage was held void against general creditors, because actually fraudulent.⁶³

§ 1260. And Mere Remaining in Possession and Selling for Short Period without Reservation of Power of Sale, Does Not Viti.—

And a chattel mortgage on a stock of goods not reserving power of sale, is not void because the mortgagors did remain in possession a short while and sell in the usual course of business.⁶⁴

59. In *re Bellevue Pipe & Fdy. Co.*, 22 A. B. R. 97, 16 Ohio Dec. 247 (Ref. Ohio).

60. *Alles v. Johansen, etc.*, 28 A. B. R. 299, 197 Fed. 274 (C. C. A. Mo.).

60a. In *re Harnden*, 29 A. B. R. 507, 200 Fed. 172 (D. C. New Mex.).

61. In *re Beede*, 11 A. B. R. 387 (D. C. N. Y.), in which case, however, attention was not particularly called to the force of § 67 (e). In *re Burnham*, 15 A. B. R. 553, 140 Fed. 926 (D. C. N. Y.); *obiter*, In *re Dry Dock Co.*, 16 A. B. R. 326 (C. C. A. N. Y.).

62. In *re Beede*, 11 A. B. R. 387 (D.

C. N. Y.); In *re Burnham*, 15 A. B. R. 553, 140 Fed. 926 (D. C. N. Y.).

63. Compare *ante*, § 1209; also, In *re Hartman*, 26 A. B. R. 76, 185 Fed. 196 (D. C. N. Y.).

64. *Davis v. Turner*, 9 A. B. R. 704, 120 Fed. 605 (C. C. A. N. Car.); In *re Standard Tel. Co.*, 19 A. B. R. 491, 157 Fed. 106 (D. C. Wis.), quoted at § 1258; *Knapp v. Milw. Tr. Co.*, 20 A. B. R. 671, 162 Fed. 675 (C. C. A. Wis., affirming In *re Standard Tel. Co.*, 19 A. B. R. 491, 157 Fed. 106). Perhaps, In *re Tucker*, 20 A. B. R. 404, 161 Fed. 584 (D. C. Ga.).

§ 1261. **Power of Sale Not Reserved in Express Terms.**—And they are void whether the power of sale be expressed in the mortgages themselves or be by outside agreement,⁶⁵ and such agreement may be inferred from acquiescence with knowledge on the mortgagee's part;⁶⁶ and the ordinary stipulation that the mortgagor may continue in full and free enjoyment has been held to mean when applied to a stock of merchandise the usual method of enjoyment, namely, sale.⁶⁷

§ 1262. **Whether Power of Sale Mortgage Void Only as to Goods to Be Sold or Void in Toto.**—In some states a chattel mortgage containing an agreement that the mortgagor may sell in the usual course of business for his own benefit is void only as to the extent of the property to which such agreement applies; thus, in Indiana;⁶⁸ also, in Vermont;⁶⁹ also in Ohio;⁷⁰ but is, perhaps, void as to the whole, in New York, by the State court rulings,⁷¹ though not by the federal rulings.⁷² Also, it is perhaps void as to the whole in Colorado.⁷³

§ 1263. **Conditional Sales Contracts with Power of Sale, Subject to Same Rules as Chattel Mortgages.**—Conditional sales contracts are ineffective in many States to reserve title in the vendor, where the conditional vendee has the power of selling in the usual course of business.⁷⁴

In re Garcewich, 8 A. B. R. 149, 115 Fed. 87 (C. C. A. N. Y.): "It is the settled law of this State that personal property may be sold and delivered

65. *Skillen v. Endelman*, 11 A. B. R. 166, 39 Misc. 261, 79 N. Y. Supp. 413; *Mitchell v. Mitchell*, 17 A. B. R. 389 (D. C. N. Car.); In re Ditsch, 17 A. B. R. 912 (D. C. Kans.); compare In re Geiver, 28 A. B. R. 413, 193 Fed. 128 (D. C. S. Dak.).

66. *Skillen v. Endelman*, 11 A. B. R. 766, 38 Misc. 261, 79 N. Y. Supp. 413; In re Ditsch, 17 A. B. R. 912 (D. C. Kas.); In re Noethen, 29 A. B. R. 234, 201 Fed. 97 (C. C. A. N. Y.).

67. In re Nat'l Bk. of Canton, 14 A. B. R. 183, 135 Fed. 62 (C. C. A. Ohio).

68. In re Soudans Mfg. Co., 8 A. B. R. 45, 113 Fed. 804 (C. C. A. Ind.).

69. In re Ball, 10 A. B. R. 564, 123 Fed. 164 (D. C. Vt.): "The referee has found that it was understood between the claimant and the bankrupt, when the mortgages were made, that he was to remain in possession of the goods, sell them in the ordinary course of the business, and use the proceeds as he needed the same. This provision is said to have rendered the mortgages fraudulent as to creditors, and void as to the trustee. But no wrongful intention is found, and the effect of the agreement itself would seem to be no more than a withdrawal of the property as fast as sold from the operation of the mortgages. * * * The mort-

gage appears to be valid as to the goods on hand when it was made."

70. In re Hammond, 26 A. B. R. 336, 188 Fed. 1020 (D. C. Ohio), quoted, on entirely distinct point, at § 1270.

71. *Skillen v. Endelman*, 11 A. B. R. 766, 39 Misc. 261, 79 N. Y. Supp. 413; apparently, *Zartman v. Nat'l Bk.*, 16 A. B. R. 155, 193 App. Div. 406, affirmed in 19 A. B. R. 27, 189 N. Y. 267; compare, In re Dry Dock Co., 16 A. B. R. 325 (C. C. A. N. Y.).

72. In re Davis, 19 A. B. R. 98, 155 Fed. 671 (D. C. N. Y.).

73. *Dodge v. Norlin*, 13 A. B. R. 176, 133 Fed. 363 (C. C. A. Colo.).

74. Inferentially, In re Carpenter, 11 A. B. R. 147, 125 Fed. 831 (D. C. N. Y.); In re Howland, 6 A. B. R. 495, 109 Fed. 869 (D. C. N. Y.); compare, *Dolle v. Cassell*, 14 A. B. R. 52, 135 Fed. 52 (C. C. A. Ohio, reversed sub nom. *York Mfg. Co. v. Cassell*, 15 A. B. R. 633, 201 U. S. 344); instance, In re Newton & Co., 18 A. B. R. 567, 153 Fed. 841 (C. C. A. Ark.); In re Geo. O. Hassam & Son, 18 A. B. R. 745, 153 Fed. 932 (D. C. Vt.), quoted at § 1228; In re Perkins, 19 A. B. R. 134, 155 Fed. 237 (D. C. Me.), quoted at § 1222½; *Mishawaka Woolen Mfg. Co. v. Westveer*, 27 A. B. R. 345, 191 Fed. 465 (C. C. A. Mich.).

under an agreement for the payment of the price at a future day, and the title by express agreement remain in the vendor until the payment of the purchase price. In such a case the payment is strictly a condition precedent, and until the performance the title does not vest in the buyer. It is one of the exceptional cases in which the law tolerates the separation of the apparent from the real ownership of chattels when the honesty of the transaction is made to appear. But when the purpose for which the possession of the property is delivered is inconsistent with the continued ownership of the vendor, the transaction will be presumed fraudulent as against purchasers and creditors. The transaction will be deemed merely colorable, and the title to have been vested absolutely in the buyer. *Ludden v. Hazen*, 31 Barb. 650; *Frank v. Batten*, 49 Hun 91, 1 N. Y. Supp. 705; *Bonesteel v. Flack*, 41 Barb. 435. When the property is delivered to the vendee for consumption or sale, or to be dealt with in any way inconsistent with the ownership of the seller, or so as to destroy his lien or right of property, the transaction cannot be upheld as a conditional sale, and is a fraud upon the creditors of the vendee. Even in the case of a chattel mortgage, when it is understood between the mortgagor and the mortgagee that the mortgagor may sell the chattels in his business, and use the proceeds, the transaction is fraudulent in law as against the creditors of the mortgagor. Such an arrangement, if expressed in the instrument, defeats its essential nature and qualities as a mortgage, so that, in a legal sense, it is not a security, but merely the expression of a confidence by the mortgagee in the mortgagor; and, if made, but not expressed in the instrument, is equally vicious, if not more suggestive of a fraudulent purpose."

But in some States, they are valid; are valid even as against assignees in insolvency; also are valid whether they be recorded or not, and so, in such States, they are good against the trustee.⁷⁵

Bryant v. Swofford Bros. Co., 22 A. B. R. 111, 214 U. S. 279, " * * * but in bankruptcy the construction and validity of such a contract must be determined by the local law of the State. * * * That such a contract is a conditional sale and is valid without record is the law of Arkansas. * * * The trustee has no higher rights in this regard."

In *re Newton* (*Swofford Bros. Dry Goods Co. v. Bryant*), 18 A. B. R. 567, 153 Fed. 841 (C. C. A. Ark.): "Whether the contract under which appellant claims is one of conditional sale or is a chattel mortgage, and, as between the parties thereto, whether it is valid, and what the effect of the failure to record it may be, are questions to be determined exclusively by the local law. *Thompson v. Fairbanks*, 196 U. S. 516, 13 Am. B. R. 437; *Humphrey v. Tattman*, 198 U. S. 91, 14 Am. B. R. 74; *York Mfg. Co. v. Cassell*, 201 U. S. 344, 15 Am. B. R. 633. Whatever may be the law in some jurisdictions it is authoritatively settled in Arkansas, that a contract of conditional sale is valid notwithstanding it contains a provision that the vendee may sell the property in the usual course of his business. *Triplett v. Implement Co.*, 68 Ark. 230, 57 S. W. 261, involved a contract of that character, and the conditional vendor was allowed to recover the goods from the vendee's assignee in insolvency who had taken possession of them." Quoted further at § 1381.

Thus, as to contracts of "sale and return."⁷⁶

In *re Dunlop*, 19 A. B. R. 361, 156 Fed. 545 (C. C. A. Minn.): "A stipula-

⁷⁵. In *re Gray*, 21 A. B. R. 375, 170 Fed. 638 (D. C. Okla.).

⁷⁶. In *re Allen*, 25 A. B. R. 722, 183 Fed. 172 (D. C. Ark.).

tion that the purchaser may sell the merchandise in the regular course of business, and that he shall apply the proceeds to his debt as a credit or as collateral security, at the option of the vendor, does not render such a contract fraudulent or voidable against creditors. It does not make it a chattel mortgage with a secret lien."

In *re Pierce*, 19 A. B. R. 662, 157 Fed. 755 (C. C. A. N. Dak.): "But the trustee says the sale was absolute, not conditional, because the bankrupt, a merchant, was authorized to resell the property in the usual course of his business. The prevailing rule, however, is that this does not destroy the title reserved by a vendor, at least before there has been a resale to a third party. The title to the articles unsold remains in the vendor until the purchase price is paid. *Lewis v. McCabe*, 49 Conn. 141, 44 Am. Rep. 217; *Rogers v. Whitehouse*, 71 Me. 222; *Armington v. Houston*, 38 Vt. 448, 91 Am. Dec. 366. In the latter case the understanding was that the vendee might use the goods for family consumption. See, also, *Swofford Bros. Dry Goods Co. v. Bryant* (C. C. A.), 18 Am. B. R. 567, 153 Fed. 841, and cases cited. Our attention has not been called to any contrary rule in North Dakota, where this controversy arose."

In *re Gilligan* (*Troy Wagon Works v. Hancock*), 23 A. B. R. 668, 152 Fed. 605 (C. C. A. Ind.): "With these cases before it—the only ones tending to support appellant's contention—and with other cases of the Supreme Court of Indiana, notably *Winchester v. Carman*, 109 Ind. 31, 9 N. E. 707, 58 Am. Rep. 382, in which the court indicates, though perhaps by obiter dicta, that the possession of property held by the retailer, for sale, would be inconsistent with continued ownership by the vendor, the Appellate Court of Indiana in *West v. Fulling* (Ind. App.), 76 N. E. 325, passed squarely upon the proposition under review, holding that an alleged contract under which the vendor sold groceries to another, authorizing the buyer to sell the same in the ordinary course of business, but reserving title until the goods were paid for, was fraudulent—the court reviewing all the Indiana cases, and some of the New York cases on the subject." This case is quoted further at § 1141.

§ 1263½. Equitable Liens and Power of Sale in Other Cases than Mortgages or Conditional Sales.—An equitable lien which involves the apparent ownership in one person who sells in the ordinary course of trade, will not be sustained as against the trustee, where it would work a fraud upon the law.⁷⁷

In *re Liberty Silk Co.*, 18 A. B. R. 582, 152 Fed. 844 (D. C. N. Y.): "But, under the authority of the same decision [*Hewitt v. Berlin Machine Wks.*] it is asserted that, inasmuch as the trustee has no better right or title to the bankrupt's property than belongs to the bankrupt or to his creditors at the time when the trustee's title accrues, the contract of August 25th, 1905, should be regarded as conferring an equitable lien—a something which is neither a mortgage nor a conditional sale, but a partial reservation of interest on the part of the vendor, not obnoxious to any law of the State of New York, and within the equity of the Bankruptcy Act as interpreted in the case last cited. It must be admitted that no actual fraud is shown or suspected in this transaction, and that the courts of this state have gone far in upholding the validity of hypothecations of personal property even where the goods hypothecated

⁷⁷ In *re Bellevue Pipe & F'dy Co.*, 22 A. B. R. 97, 16 Ohio D. C. 247 (Ref. Ohio).

were to be turned into money by the mortgagor, bailee, or conditional vendee, provided it was also agreed that the proceeds of such sale or use were to be applied in diminution of the debt secured by the goods themselves. *Prentiss Toll, etc., Co. v. Schirmer*, 136 N. Y. 304, 32 N. E. 849, 32 Am. St. Rep. 737. But I am not aware that it has been doubted since *Southard v. Benner*, 72 N. Y. 424, that where a right existed in a chattel mortgagor to sell the mortgaged property and use the proceeds thereof generally in his own business is, however honest in intent, a fraud upon the law. The wholesome rule is summarily stated *In re Garcewich*, 8 A. B. R. 149, 115 Fed. 87, that when property is delivered to a vendee for consumption or sale, or to be dealt with in any way inconsistent with the ownership of the seller, the transaction cannot be upheld as a conditional sale and is a fraud upon the creditors of the vendee. That rule in my judgment applies to this case. While I think as above indicated that the transaction is really a mortgage, and as such void for want of filing, yet it makes no difference whether it be denominated in one way or another it still remains true that the filatures in question were delivered to the bankrupt with obvious intent that they should be used and consumed in the ordinary course of that bankrupt's business, and for the benefit thereof. Secret liens are to be discouraged, and where, even innocently, vendors seeking to create such liens permit so obvious a badge of fraud as here appears to exist in their contracts, they must take the legal consequences, and the matter is not bettered by name. An equitable lien which involves a fraud upon the law is none the less obnoxious because so different in form from the better known mortgage or conditional sale as hardly to fall under either well-known category."

§ 1264. Mortgages on After-Acquired Property.—This subject is involved in many other subjects elsewhere discussed.⁷⁸

§ 1264½. Transfers by Insolvent Corporations to Secure Preferred Stockholders.—When a corporation is insolvent it cannot transfer its assets to secure preferred stockholders. They are not creditors and so the transfer is not a preference, though void on grounds of public policy.⁷⁹

§ 1265. Peculiar Rights or Remedies of Creditors by Special Statute, Trustee Succeeds Thereto.—Where the peculiar laws of a State give creditors special rights or remedies, the trustee in bankruptcy succeeds to the same rights or remedies.⁸⁰

78. See various sub-titles: "Seventh Element of a Preference," § 1371; "Taking of Possession of After-Acquired Property Curing Lack of Record," ante, § 1236. As to general effect of the bankruptcy law upon the title to after-acquired property, see general discussion, ante, § 1139, et seq.; "After-Acquired Property Coming under Chattel Mortgage," ante, § 1199.

79. *Spencer v. Smith*, 29 A. B. R. 120, 201 Fed. 647 (C. C. A. Colo.).

80. Instance, *Union Trust Co. v. Amery*, 27 A. B. R. 499 (Sup. Ct.

Wash.); *In re Jacobs*, 1 A. B. R. 518 (D. C. La.); *Andrews v. Mather*, 9 A. B. R. 296, 134 Ala. 358.

Instances of trustee's subrogation to creditor's peculiar rights:

1. **Statutory Provision That Property Consigned to Factor or Agent Who Does Not Designate His Capacity, Goes to All Creditors on Insolvency.**—Thus, where the State law says the property consigned to a factor, agent, etc., who does business in his individual name without adding "factor" or "agent" thereto, shall on his insolvency, go into the general estate for all creditors, such rights

§ 1266. But Where Special Rights Dependent on Special Remedies Not Available Because of Bankruptcy.—But where the property involved is already in the custody of the bankruptcy court and such special rights are not given as matter of substantive law but are wholly dependent

inure to the trustee in bankruptcy. *Chesapeake Shoe Co. v. Seldner*, 10 A. B. R. 466, 122 Fed. 593 (C. C. A. Va.).

2. **Conditional Sales Wholly Void.**—"Conditional Sales" are void in Pennsylvania as to creditors. In re *Butterwick*, 12 A. B. R. 536, 131 Fed. 371 (D. C. Pa.).

3. **Spendthrift Trusts.**—"Spendthrift Trusts" in New York: surplus of income beyond sum necessary for education and support of beneficiary, is liable to creditors on institution of equity suit: the trustee may institute such suit. In re *Tiffany*, 13 A. B. R. 310, 133 Fed. 799 (D. C. N. Y.); *Brown v. Barker*, 8 A. B. A. 450 (N. Y. Sup. Ct. App.); In re *Baudouine*, 3 A. B. R. 656, 101 Fed. 574 (C. C. A. N. Y.). But compare, In re *McKay*, 16 A. B. R. 238 (D. C. N. Y.).

But "Spendthrift" trusts in Massachusetts are held not to pass where the will directs that it shall not be assignable nor subject to levy nor seizure by creditors. *Munroe v. Dewey*, 4 A. B. R. 264 (Mass. Sup. Jud. Ct.).

4. **Vitiation of Execution Levy by Using It as Mere Security.**—In Pennsylvania an execution levy is vitiated by using it as a means of compelling payments on account from time to time, after levy made, using it thus as a security rather than as a means of satisfaction by sale and application of proceeds. In re *Thackara*, 15 A. B. R. 258, 140 Fed. 126 (D. C. Pa.).

5. **Preferential transfer in contemplation of insolvency under New York State Stock Corporation Law.** *Wright v. Gansevoort Bk.*, 17 A. B. R. 326 (N. Y. Sup. Ct.); *Wright v. Gansevoort Bank*, 18 A. B. R. 363, 118 App. Div. 281; *Gill v. Bells' Knitting Mills Co.*, 21 A. B. R. 282 (N. Y. Ct. App.). Bona fide purchaser for value protected. *Perry v. Van Norden Trust Co.*, 20 A. B. R. 190 (N. Y. Ct. App.).

6. **Unfiled Bill of Sale under New York Personal Property Law.**—In re *Schlessel*, 18 A. B. R. 434 (Ref. N. Y.).

7. **"Void as to Creditors," Meaning in One State Judgment Creditors, Not Necessarily Levying Creditors.**—Chattel mortgages not recorded "void as to creditors" means judgment creditors but not necessarily levying

creditors, in New York. *Gove v. Morton Trust Co.*, 12 A. B. R. 297, 96 N. Y. App. Div. 177; *Zartman v. Nat'l Bk.*, 16 A. B. R. 157, 106 App. Div. 406 (N. Y.); compare, In re *Beede*, 11 A. B. R. 387 (D. C. N. Y.).

8. **Void as to "Interested Parties."**—Trustee held to be "interested." In re *Hickerson*, 20 A. B. R. 682, 162 Fed. 345 (D. C. Idaho).

9. **Simple Contract Creditors in Some States Competent to Set Aside Fraudulent Conveyance.**—Where State law permits simple contract creditor to maintain suits to set aside fraudulent conveyances, the trustee has the same right. *Andrews v. Mather*, 9 A. B. R. 300, 134 Ala. 358; *Grunsfeld Bros. v. Brownwell*, 11 A. B. R. 601 (Sup. Ct. N. Mex.).

10. **Intermediate Creditors' Rights Where Chattel Mortgage Withheld from Record.**—Chattel mortgages eventually filed but meanwhile withheld from record are void as to simple contract creditors becoming such in the interval before the filing, in New York, and in Missouri, and are hence void as to the trustee where such creditors exist. In re *Metropolitan Co.*, 15 A. B. R. 119 (Ref. N. Y.). In re *Martin*, 23 A. B. R. 151, 173 Fed. 597 (C. C. A. Mo.).

Likewise in South Carolina, *Simmons v. Greer*, 23 A. B. R. 443, 174 Fed. 654 (C. C. A. S. Car.), quoted at § 1225½.

11. **Rights as between Subsequent and General Creditors Where Mortgage, Voidable Only as to Subsequent Creditors, Is Set Aside.**—Subsequent creditors' rights on setting aside a mortgage void as to subsequent creditors alone, for non-record: Thus, where the State law makes a chattel mortgage invalid as to subsequent creditors, whether contract or judgment creditors, unless it is recorded within forty days of its execution or delivery the fund derived by the trustee from the sale of the chattels covered by it is to be divided pro rata amongst subsequent creditors, the balance to apply on the mortgagee's claim and remainder if any to preceding creditors. In re *Cannon*, 10 A. B. R. 64, 121 Fed. 582 (D. C. S. Car.).

And where such a mortgage has

upon the creditors' resorting to a certain form of litigation for remedy, as by statutory suits to set aside fraudulent or preferential conveyances that must be brought and carried on in prescribed forms and within prescribed time in order to confer the rights, such rights, from necessity, cannot (un-

eventually been filed, though thus improperly withheld for a time, only creditors becoming such in the meantime may share in the proceeds, the mortgage being good as to all others. *Simmons v. Greer*, 23 A. B. R. 443, 174 Fed. 654 (C. C. A. S. Car.), quoted at § 1225¾.

12. **Transfer Set Aside, All Creditors to Participate, Not Simply Those Existing at Time of Transfer.**—In Ohio, on the setting aside of the transfer, all creditors are to participate in the proceeds; not simply those existing at time of the transfer. In re *Kohler*, 20 A. B. R. 89, 159 Fed. 871 (C. C. A. Ohio), quoted at § 1225¾.

13. **Unrecorded Chattel Mortgage Void as to Intervening General Creditors—When Set Aside in Bankruptcy Intervening Creditors Alone Participate.**—In Missouri a chattel mortgage withheld from record for a period but filed before bankruptcy, is void as to intervening creditors whether "armed" or not and hence is void as to the trustee; but on being set aside, the proceeds are distributed among the intervening creditors. In re *Martin*, 23 A. B. R. 151, 173 Fed. 597 (C. C. A. Mo.).

14. **All Mortgages within Three Months of Failure, by State Statute Presumptively Fraudulent unless Rebutted by Proof of Present Real Consideration.**—Thus, where the Civil Code of Louisiana makes null and void as presumptively fraudulent all mortgages given within three months of a debtor's failure, unless the mortgagee shall prove that at the moment of the contract he gave a real and effective value for it, such provision is incorporated into the bankruptcy act. In re *Jacobs*, 1 A. B. R. 518 (D. C. La.).

15. **No Evasion of Statute Requiring Recording within Six Months of Execution, by Keeping Renewals Off Record.**—State statute requiring mortgages to be recorded within six months of execution cannot be evaded by giving renewals thereof within every six months and keeping the renewals off the record, even though the last one be recorded within the six months and before bankruptcy.

In re *Noel*, 14 A. B. R. 715, 137 Fed. 694 (D. C. Md.).

16. **"Warehouse" Receipts—Insufficient "Warehousing" Where Merely Space in Bankrupt's Own Warehouse Rented.**—It is an insufficient "warehouse" under the Wisconsin Statute to secure the benefits of warehouse receipts, to simply rent space in the bankrupt's warehouse. *Warehouse Co. v. Hand*, 16 A. B. R. 49 (C. C. A. Wis.); *Warehouse Co. v. Hand*, 19 A. B. R. 291, 206 U. S. 415. Compare, ante, § 1146.

17. **Resident Creditors' Claims Having Priority Over Claims of Foreign Corporation.**—The Tennessee statute gives priority, in the distribution of the assets of a foreign corporation, to the claims of resident creditors over the claims of other foreign corporations which have not complied with the statutory regulations for the doing of business by foreign corporation; and this priority has been recognized in bankruptcy, as conferring substantive rights, not dependent upon resort to special remedies. In re *Standard Oak Veneer Co.*, 22 A. B. R. 883, 173 Fed. 103 (D. C. Tenn.), quoted at § 2196.

18. **"Sales of Merchandise in Bulk."** Under Maine Act, which does not declare fraudulent in law sales in bulk not conducted in compliance with the Statute, a bona fide purchaser was held protected, where the purchase price was used in paying creditors. *Gorham v. Buzzell*, 24 A. B. R. 440, 178 Fed. 596 (D. C. Me.).

Such sales, where the purchaser is innocent of participation in any fraudulent intent, will not be void (in the absence of any statute regulating the same). *Shelton, Trustee, v. Price*, 23 A. B. R. 431, 174 Fed. 891 (D. C. Ala.).

19. **Conditional Sale Becoming Absolute on Failure to Record Within Ten Days.**—Where a State statute makes a conditional sale absolute as to subsequent creditors for failure to register within a certain time, the trustee has been held to succeed to the rights of subsequent creditors. In re *American Machine Works (Chilberg v. Smith)*, 23 A. B. R. 483, 174 Fed. 805 (C. C. A. Wash.).

20. **Consent of Two-Thirds of Stock-**

less such statutory suits are instituted) be applied in determining the validity of liens and interests on the property so in the custody of the bankruptcy court and in course of administration and distribution in the bankruptcy proceedings.⁸¹

Impliedly, *In re Terrill*, 4 A. B. R. 145 (D. C. Vt.): "They were mere preferences which would become void by insolvency proceedings if begun within a required time, and might not be, and in fact were not begun at all."

Compare, inferentially and apparently, but not really contra, *In re Boyd*, 10 A. B. R. 340, 120 Fed. 999 (D. C. Iowa): "It is a familiar rule that, when property comes under the control and custody of a court, all parties claiming interests or rights thereto will be permitted to assert such rights before the court having the custody of the property. It is equally well settled that in such cases regard will be paid and protection be granted to the substance of the right asserted, even though the court may not be able to adopt and follow the form of the remedy, which under the laws of the State, would be alone open to the claimant if the property was not in the custody of the court."

Compare, obiter and inferentially, *Goldman v. Smith*, 1 A. B. R. 271, 93 Fed. 182 (D. C. Ky.): "Where there is a preference prohibited by the Kentucky Statute, it does not of itself make the preference a general assignment but requires some proceedings in the State court to have it so declared: hence we have not regarded it as applicable to the question under consideration."

But it has been held that if such special remedies have already been resorted to, or are still available and are actually availed of, then the special rights thereby conferred are to be recognized in bankruptcy, and if the

holders to Renewal of Chattel Mortgage.—By statute, in New York, a renewal of a chattel mortgage for money borrowed, not for purchase price, by a corporation, is invalid without the consent of two-thirds of the stockholders, and it has been held that the trustee succeeds to the rights of these creditors, though the corporation may be estopped. *In re Laundry Co.*, 23 A. B. R. 859, 176 Fed. 740 (D. C. N. Y.), which would be, perhaps, good law if occurring since the Amendment of 1910, whereby the trustee has been given the rights of creditors holding executions, but is doubtful law as applied to the situation before the Amendment of 1910, when the trustee was held simply to stand in the shoes of the bankrupt and to be bound by the bankrupt's estoppels, § 1149.

21. Lien Acquired by Delivery of Execution to Sheriff. Thus where, under the local law, a lien is acquired by the delivery of an execution to the sheriff, the trustee may be subrogated to such lien creditors' rights. *Rock Island Plow Co. v. Reardon*, 27 A. B. R. 492, 222 U. S. 534, affirming 22 A. B. R. 26.

22. Right of Action against Officers of Corporation, under a local statute, vests in the trustee. *In re Swofford Bros. Dry Goods Co.*, 25 A. B. R. 282, 180 Fed. 549 (D. C. Mo.).

81. *In re Porterfield*, 15 A. B. R. 11 (D. C. W. Va., reversed sub nom. *Moore v. Green*, 16 A. B. R. 648, 145 Fed. 480); compare, also, *Pollock v. Jones*, 10 A. B. R. 616, 124 Fed. 163 (C. C. A. S. Car., affirming 9 A. B. R. 262). See post, §§ 2196, 2197.

Statute Requiring Tender Back of Part of Purchase Price on Retaking Possession under Conditional Sale.—

It has been held in Ohio that the statute requiring the conditional vendor to refund a part of the purchase price before taking possession of conditionally sold property, does not apply where the conditional vendor does not seek to regain possession thereof from the bankruptcy court, but asks the bankruptcy court merely to sell the property and pay him his lien from the proceeds or to compel the trustee to complete the contract. *In re Max Goldman*, 23 A. B. R. 497, 174 Fed. 579 (C. C. A. Ohio).

State statute confines the benefit to certain ones to the exclusion of all others such persons will have the same priority in bankruptcy.⁸²

§ 1267. Maintaining Statutory Suits, to Perfect Special Rights, but for Benefit of All.—Perhaps in such cases the bankruptcy court might permit the creditors for the benefit of all to institute litigation or to continue litigation already instituted in the State court, retaining, itself, the custody of the res, under the analogous doctrine of *In re Johnson*, 11 A. B. R. 544 (D. C. Nev.); *In re Mundle*, 14 A. B. R. 680, 139 Fed. 691 (D. C. N. Y.); *Crosby v. Spear*, 11 A. B. R. 613, 98 Me. 542; *Chauncey v. Dyke Bros.*, 9 A. B. R. 444, 119 Fed. 1 (C. C. A. Ark.); *Vollkommer v. Frank*, 14 A. B. R. 695; *Small v. Muller*, 8 A. B. R. 448 and others; not confining the benefits to certain creditors, however, as seems to be the suggestion in *Moore v. Green*, 16 A. B. R. 648, 145 Fed. 480 (C. C. A. W. Va.), wherein the court say,

"As to whether the relief to which the petitioner herein is entitled should have been afforded him by proceedings in the bankruptcy court, or that court should have suspended its administration so far as the portion of the assets of the bankrupt is concerned, properly applicable to the lien of the deed of the 13th day of June, 1902, in favor of Mrs. Porterfield, is largely a matter of discretion in the view we take. Either course could have been adopted. No question of jurisdiction was involved. The bankruptcy court clearly had jurisdiction to proceed, and, if needs be, to have stayed the prosecution of the suit in the State court for the time being; but the State court likewise, at the time of the institution of the suit therein and the commencement of the bankruptcy proceedings, had and still has jurisdiction, and we think, as a matter of convenience, aside from any question of comity, the better plan would have been and is to proceed with the litigation in the State court, to the end that all creditors who may desire to do so may appear therein, and assert their rights to such fund, and in the meantime the bankruptcy proceedings would as to that portion of the estate remain in abeyance; the bankruptcy court carrying out the judgment of the State court, when duly informed thereof, in said proceeding."

But, of course, it is not bound to do so and it may refuse to permit such controversy over property in its own custody to be carried on elsewhere.⁸³

^{82.} *Moore v. Green*, 16 A. B. R. 648, 145 Fed. 480 (C. C. A. W. Va., reversing *In re Porterfield*, 15 A. B. R. 11): In this case a mortgage to secure a pre-existing debt was made by an insolvent before four months prior to the institution of bankruptcy proceedings against the mortgagor; but between the time of its execution and the bankruptcy a creditor started suit in the State Court under a State statute declaring, upon suit instituted within a year, such conveyances should be held to inure to the benefit of all creditors joining. The court held that the legal proceedings in the State

court did not create the lien but simply perfected the lien for all creditors joining and that the creditors thus joining were entitled to priority under § 64 (b) (5) and should have distribution made in accordance with the State statute. But compare, §§ 1225¾, 1738.

^{83.} *In re Mertens*, 12 A. B. R. 698, 131 Fed. 507 (D. C. N. Y.); *In re Porterfield*, 15 A. B. R. 11, 138 Fed. 192 (D. C. W. Va., reversed on other grounds sub nom. *Moore v. Green*); *Moore v. Green*, 16 A. B. R. 648, 145 Fed. 480 (C. C. A. W. Va.).

§ 1268. And Where Bankruptcy Court Not in Custody of Property Involved.—Where the bankruptcy court has not the custody of the property involved, the question as to what rights the creditors will acquire under such statutes will depend upon several things: 1st, Undoubtedly, if the trustee or creditors would not be permitted by the State courts to turn the property or its proceeds on recovery over to the bankruptcy court for distribution in accordance with the Bankruptcy law, then the trustee and creditors would not be permitted to commence such suit, nor to maintain one already commenced. 2nd, Probably, also, if the state statute declares that the setting aside of such conveyance shall operate as an assignment for the benefit of creditors, then a substantive right would exist independently of the remedy, in which event the trustee probably would be subrogated to the rights of creditors under such a statute, even if not permitted to avail himself thereof because of the form of the remedy prescribed.⁸⁴

And it has been held that where a transfer is not preferential as against the Bankrupt Act, but is preferential by State law, the trustee may intervene in behalf of all creditors in the pending suit in the State court, and the lien of such suit may be preserved for the benefit of the estate in bankruptcy though annulled as to the particular creditors instituting the suit, such being the holding in a State where the State law declares a transfer by an individual member of a partnership, of his individual property, to be a preference as against partnership creditors of an insolvent partnership, contrary to the rule in bankruptcy.⁸⁵

§ 1269. Prior General Assignment—Whether Effective to Avoid Liens Recorded before Bankruptcy but Not until after Assignment.

—Where the State law gives to a general assignment for the benefit of creditors the effect of a levy of execution or attachment so as to avoid unrecorded liens, such liens if not recorded at the time of the assignment although subsequently recorded before the bankruptcy have been held in one case to be void as against the trustee although the assignment itself is nullified by the bankruptcy.

In *re Andrae Co.*, 9 A. B. R. 135, 117 Fed. 561 (D. C. Wis.): "By statute, in Wisconsin, the assignee in such case represents the rights and interests of creditors in respect of transfers or liens which are fraudulent or void as to creditors, and such right is enforceable by a creditor if not enforced by the assignee. * * * As the mortgage was not a valid lien against creditors when their rights accrued under the assignment, it is plain that the subsequent filing gave it no better standing within the State Law. It was equally invalid, under this provision of the Bankruptcy Act, when the petition for involuntary bankruptcy was filed, March 15th; unless that act operates through some of its other provisions to divest the creditors of such right, and thus enables the parties to the void instrument to give it validity by their mere act of filing on

⁸⁴. But compare, obiter (as to act of bankruptcy), *Goldman v. Smith*, 1 A. B. R. 271, 93 Fed. 182 (D. C. Ky.).

⁸⁵. *Miller v. Acid & Fertilizer Co.*, 21 A. B. R. 416, 211 U. S. 496, quoted at §§ 1441, 1489, 1491.

the intermediate day. I am of opinion that neither the terms of the Bankruptcy Act nor intervention thereunder have such anomalous result. True, the making of the assignment was an act of bankruptcy within the act, * * * but the assignment was not void, and, except for the adjudication of bankruptcy, the assignment would have remained in force to be carried out under the State law. It was voidable only; in force when this petition was filed and until displaced by the adjudication thereupon. * * * So considered, the subsequent filing was nugatory, and the mortgage is within § 67a, and not a valid lien against the estate."

Where a prior general assignment is, by State law, effective to avoid unrecorded liens, it will be likewise effective in bankruptcy if the lien be preserved for the benefit of the estate. This proposition is fully discussed post, at § 1489.

However, the principle of this section seems to have been violated in a case where a trust mortgage which operated like an assignment for the benefit of creditors and hence was avoided by the bankruptcy, and as to which unfiled chattel mortgages were by State law void, was given before an unfiled mortgage was finally filed, the giving of the trust mortgage and also the subsequent filing of the chattel mortgage occurring within four months of the bankruptcy; the court refusing to preserve the lien of the trust mortgage for the benefit of all creditors, but declaring it, instead, void for all purposes.^{85a}

§ 1269½. Anti-Bulk-Sales Laws.—Most of the States have in recent years adopted legislation regulating the sales of entire stocks in bulk. In general the trustee succeeds to these rights of creditors, under § 67.⁸⁶

It has been held that the Maine Anti-Bulk-Sales Act does not make such a sale fraudulent in law for non-compliance with the statute, so that where no fraud in fact is shown and the proceeds have been used in paying creditors, the trustee may not recover against the purchaser.⁸⁷

SUBDIVISION "C."

TRUSTEE AS A CREDITOR "ARMED WITH PROCESS"—AMENDMENT OF 1910.

§ 1270. Trustee Now a Creditor "Armed with Process"—Amendment of 1910.—As previously remarked at §§ 1137 and 1207, the Amendment of 1910 to Bankruptcy Act, § 47 (a) (2), endows the trustee with the rights and remedies of a creditor "armed with process." These rights are additional to those previously enjoyed by him and creditors are thereby armed under the Bankruptcy Act of 1898 with more extensive rights and remedies than under any previous bankruptcy law of the United States or of England. The trustee's rights under this amendment are not derivative;

^{85a} *Rouse v. Ottenwess & Huxoll*, 31 A. B. R. 115, 208 Fed. 881 (C. C. A. Michigan).

⁸⁶ *In re Rosenberg*, 22 A. B. R. 900 (Ref. N. Y.). Compare, *In re*

Lipman, 29 A. B. R. 139, 201 Fed. 169 (D. C. N. J.). Also, see post, §§ 1494, 1495, 1496.

⁸⁷ *Gorham v. Buzzell*, 24 A. B. R. 440, 178 Fed. 596 (D. C. Me.).

they are not those derived from any existing creditor. They are independent rights conferred by the statute itself. They effectually invest the trustee as representative of the creditors with all the possible rights of creditors under state law. He is in effect erected by the statute into an ideal "creditor"—one might say into all kinds of a creditor, having all rights possible to a creditor under State law.

So the trustee, as to all property in the custody or coming into the custody of the bankruptcy court, is, in addition to his other rights, to be deemed vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon; and also as to all property not in the custody of the bankruptcy court is to be deemed vested with all the rights, remedies and powers of a judgment creditor holding an execution duly returned unsatisfied.⁸⁸

In *re Farmers' Co-Op. Co. of Barlow* No. 1, 30 A. B. R. 187, 207 Fed. 108 (D. C. N. Dak.). "The trustee in bankruptcy derives his right from § 47a, subdivision 2, as amended by the Act of 1910. The purpose of the amendment is now reasonably clear. Under the original act several of the Circuit Courts of Appeal had held that the filing of the petition in bankruptcy amounted to a seizure of the property of the bankrupt and conferred upon the trustee the same rights as a creditor would have obtained by the levy of an execution or attachment at the date of the filing of the petition. But in *York Mfg. Co. v.*

88. See post, § 1208; also see In *re Whatley Bros.*, 29 A. B. R. 64, 199 Fed. 326 (D. C. Ga.); In *re Freedman*, 29 A. B. R. 135 (Ref. Pa.); In *re Reynolds*, 29 A. B. R. 145, 203 Fed. 162 (D. C. Ky.); *Kraver v. Abrahams*, 29 A. B. R. 365, 203 Fed. 782 (D. C. Pa.); In *re Jacobson & Perrill*, 29 A. B. R. 603, 250 Fed. 812 (D. C. Ga.); In *re Riehl*, 29 A. B. R. 613, 200 Fed. 455 (D. C. Md.); In *re Harrington*, 29 A. B. R. 690 (Ref. Mass.); In *re Merry*, 29 A. B. R. 829, 201 Fed. 369 (D. C. Me.); In *re Nuckols*, 29 A. B. R. 867, 201 Fed. 437 (D. C. Tenn.); In *re O'Callaghan*, 30 A. B. R. 97 (Ref. Mass.); In *re Morris*, 30 A. B. R. 319, 204 Fed. 770 (C. C. A. N. Y.).

Compare, In *re Snelling*, 29 A. B. R. 817, 202 Fed. 259 (D. C. Mass.), affirmed sub nom. *Clark v. Snelling*, 30 A. B. R. 50, 205 Fed. 240 (C. C. A. Mass.); *Hart v. Emmerson-Brantingham Co.*, 30 A. B. R. 218, 203 Fed. 60 (D. C. Mo.); In *re Rutland & Perry Co.*, 30 A. B. R. 383, 205 Fed. 200 (D. C. S. Car.); In *re Suit & Cloak Co.*, 28 A. B. R. 818, — Fed. — (D. C. Colo.); In *re Jacobson and Perrill*, 29 A. B. R. 603, 200 Fed. 812 (D. C. Ga.); In *re Dunn*, 28 A. B. R. 127, 193 Fed. 212 (D. C. Ark.); In *re Gaglione & Son*, 28 A. B. R.

694, 200 Fed. 81 (D. C. Pa.); *Sattler v. Slonimsky*, 28 A. B. R. 729, 199 Fed. 592 (D. C. Pa.); In *re Lorch & Co.*, 28 A. B. R. 784 (D. C. Ky.); *Big Four Implement Co. v. Isom Wright*, 31 A. B. R. 125, 207 Fed. 535 (C. C. A. Kans.); In *re Hartdagen*, 26 A. B. R. 532, 189 Fed. 546 (D. C. Pa.), quoted at § 1242; In *re Calhoun Supply Co.*, 26 A. B. R. 528, 189 Fed. 537 (D. C. Ala.), quoted at § 1242; In *re Gehris-Herbine Co.*, 26 A. B. R. 470, 188 Fed. 502 (D. C. Pa.); In *re Sterne & Levi*, 26 A. B. R. 535, 190 Fed. 70 (D. C. Tex.); In *re Nelson*, 27 A. B. R. 272, 191 Fed. 233 (D. C. S. Dak.), quoted at § 1146; In *re Downing*, 27 A. B. R. 309, 192 Fed. 683 (D. C. N. Y.), quoted at § 1415; In *re Kreuger*, 27 A. B. R. 623, 196 Fed. 705 (D. C. Ky.); In *re Merry*, 29 A. B. R. 829, 201 Fed. 369 (D. C. Me.); In *re King Motor Car Co.*, 31 A. B. R. 172 (Ref. Mich.).

Apparently contra, In *re Flatland*, 28 A. B. R. 476, 196 Fed. 310 (C. C. A. Wash.); contra [notwithstanding Amendment of 1910, conditional sale contract held valid as being a "priority" under Bankr. Act, § 64 (b) (5)]; In *re Lausman*, 25 A. B. R. 186, 183 Fed. 647 (D. C. Ky.), distinguished in *re Lorch*, 28 A. B. R. 784, 199 Fed. 944 (D. C. Ky.).

Cassell, 201 U. S. 344, 15 A. B. R. 633, the Supreme Court held these decisions to be unsound, and ruled that the trustee simply stood in the shoes of the bankrupt, and took the property subject to every claim that could have been urged against him. The trustee, therefore, as the amendment plainly declares, 'as to all property in the custody or coming into the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon.' This language measures the right of the trustee. The history of the statute, as above outlined, shows that those rights are obtained by the filing of the petition in bankruptcy. That act is by the amendment given the same force as a seizure of the property under execution or attachment by a creditor, and cannot be given any retroactive effect. In *re Jacobson & Perrill* (D. C. Ga.), 29 A. B. R. 603, 200 Fed. 812. If a creditor had levied upon the property here involved at the date of the filing of the petition, he would have acquired no rights as against the plow company, because it had filed its contract some time before; and the trustee, by the very language of the statute, has no higher right than such a creditor."

In *re Hammond*, 26 A. B. R. 336, 188 Fed. 1020 (D. C. Ohio): "If it were not for the amendment of 1910 we would be referred for determination of the question before us to section 70 of the Bankruptcy Act, which read then as now: 'The trustee of the estate of a bankrupt * * * shall * * * be vested by operation of law with the title of the bankrupt as of the date he was adjudged a bankrupt.' And, following the authority of *York v. Cassell*, it would transpire that, none of the creditors of Hammond having reduced his claim to judgment, the decisions cited above from the Ohio authorities would have no application and Fee could enforce his lien as if the bankruptcy petition had not been filed, for, under the Ohio authorities, the mortgage was good between the parties, and, by the language of the Bankruptcy Act, just quoted, manifestly the trustee stood in the shoes of the bankrupt, *York v. Cassell* being to the effect that only creditors who have reduced their claims to judgment or who have levied by attachment may assert rights against the mortgagee of a mortgage void in the particulars referred to. But the Act of June 25, 1910, amending the Bankruptcy Law, adds to § 47, paragraph (a), these words: 'And such trustees, as to all properties in the custody or coming into the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon, and also, as to all property not in the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies and powers of a judgment creditor holding an execution duly returned unsatisfied.' It seems that this language might have found a more appropriate place in § 70 of the act, but, however that may be, it is plain that the two sections must now be construed together and that the trustee can no longer be said to have the limited title of the bankrupt; wherefore it need not be argued further that, if this mortgage had been made after the amendment, Fee would have had no lien against the trustee. And we think that the amendment effects the same result in this case, although the mortgage is prior in time.

"At any time before or after the adoption of the amendment, any creditor, by reducing his claim to judgment and levying or by suing out an attachment, could have defeated Fee's mortgage. At all times it was in peril of the individual action of Hammond's creditors in this way. The Amendment of 1910 does nothing more under these circumstances than to collectively put these creditors into the position of judgment or attaching creditors by representation. It simply offers another method of effecting a remedy against the mortgage, which already existed, in behalf of the creditor."

In re Williamsburg Knitting Mill, 27 A. B. R. 178, 190 Fed. 871 (D. C. Va.): "The amended act of June 25, 1910, was passed as a result of the decision in the York Mfg. Co. case, 201 U. S. 344, 15 A. B. R. 633, and with a view of meeting the same. * * *

"The language used in this Amendment is clear and comprehensive, and as viewed by the court unequivocally gives to the bankruptcy proceeding the effect of a lien, as is contemplated by the York case, *supra*, and the same will suffice to give to those claiming rights by reason of the bankruptcy court proceedings, precedence over an unrecorded vendor's lien under the Virginia statute. The amendment does, in fact, give to the bankruptcy proceedings the force of a 'caveat to all the world,' and in effect 'an attachment and injunction,' and the same applies to cases as well of the attempted disposition of property after bankruptcy, as to those asserting title to or lien upon the bankrupt's estate arising out of transactions antedating the bankruptcy. The effect of this change is unquestionably radical and far reaching, as regards the consequence of the institution of bankruptcy proceedings, but it is what Congress had the right to do, and carries out what in the judgment of many should be the effect of such proceeding. It makes the date of the institution of the bankruptcy proceeding, the time as of which rights to, and claims against the estate, should be reckoned with and adjusted, and from and after which period no one creditor or claimant can secure or receive preference or advantage over another. The opinion of Mr. Justice Swayne in *Bank v. Sherman*, 101 U. S. 403, 406, 25 L. Ed. 866, *supra*, is particularly appropriate in this respect, the learned justice saying:

"The statute is clear and imperative. Its constitutional validity is not questioned. It contains no qualifications. We cannot interpolate what is claimed. Such a function is beyond the sphere of our power and duty. It is our business to execute the law as we find it, and not to make or modify it. In the disposition of property among creditors, equality is equity. It was the genius and purpose of the statute to secure this result as far as possible from the moment its aid was invoked, whether by debtor or creditor."

"This view of the effect of this amendment is taken by Remington, an author of recognized authority on bankruptcy laws. In the recent edition of his work (volume 3, p. 331), the author says:

"By the Amendment of 1910 to the Bankruptcy Act, § 47a (2), "this rejected doctrine" that bankruptcy operates as an "equitable levy" as to property in the custody of the bankruptcy court, has become the accepted doctrine."

"Moreover, this author shows that Congress by the amendment in question purposely sought to modify the decision of *York Manufacturing Co. v. Cassell*, *supra*. At page 331 of the same volume (3) the report of the Senate judiciary committee on the amendment of the act is set out in full, stating in terms that its object and purpose was to meet the decision in the York case, and to adopt in lieu thereof the views herein taken. Collier on Bankruptcy (8th Ed.), pp. 541, 542, refers to this amendment approvingly, and in effect takes the same view of the act that Remington does, though he calls attention to the fact that more logically the amendment should have been to § 70 of the Bankruptcy Act, instead of § 47.

"The only decision since the amended act to which the court's attention has been called is that of *In re Lausman* (D. C., Ky.), 25 Am. B. R. 186, 183 Fed. 647, a decision of Judge Evans, of the Western District of Kentucky. This opinion is entitled to much weight by reason of the recognized ability and experience of the judge rendering the same. The case involved, however, a small amount, and it is fair to assume was not presented as fully as has been

the case here, and was decided before the publication of the recent editions of Remington and Collier, the former of which called special attention to the reason for the Senate's action, as above indicated.

"It is earnestly insisted that the amended act, if given the interpretation herein accorded it, is unconstitutional as depriving the petitioners of their property without due process of law. With this view the court cannot agree, as it is in no respect a violation of one's constitutional rights to require him to conform to the recordation acts of the State in which he has property. The vendor's rights in this case would, under the plain terms of the Virginia statute, have been protected against the bankrupt's execution or other lien creditors, and remained unaffected by bankruptcy proceedings, had they seasonably complied with the statute requiring recordation of their reservation of title. The further suggestion is made that the amended act should not be given the effect contended for because of the particular section amended; in other words, it is maintained that the amendment should have been to § 70, subsection 5, instead of to clause 2 of section 47, subd. 'a' of the act. Unquestionably the amendment should more properly have been to the seventieth section of that act, as claimed, which deals with the property as to which the trustee acquires title, instead of section 47, which relates more particularly to the duties of the trustee, but at the same time it does not follow that it should have been necessarily so made, and that Congress could not have expressed its desires and wishes as well under the section prescribing the duties of the trustee as that relating to title to property, and this is just what it apparently did, and in terms so clear, comprehensive, and specific that there can be no serious doubt as to its meaning, intention, and purpose, and the court feels bound by the plain import of the language used.

"The action of the referee sought to be reviewed will be approved and affirmed."

Millikin v. Second Nat'l Bank of Balt. 30 A. B. R. 477, 206 Fed. 14 (C. C. A. Md.), reversing 29 A. B. R. 613:

"Prior to the enactment of the amendment of June 25, 1910, a trustee in bankruptcy in so far as the rights of the bankrupt were concerned stood in the shoes of the bankrupt, and the property taken by him was subject to the enforcement of any rights or equities that could have been enforced between the parties at the time of the adjudication, and at that time the principles contended for by counsel for appellee would have applied to a case like the one at bar. In other words, an unregistered mortgage being good *inter partes* could have been enforced as such, but the act as amended completely changed the situation, and now the trustee is the representative of all the creditors, thus accomplishing what the law intended, to wit, to cut up by the roots all secret liens or other agreements between the parties. Under the old law a general creditor was not permitted to contest such transactions, and as a result was deprived of the right to share in an equal distribution of the assets of the bankrupt.

"Under the present law (§ 47, subd. 2) a trustee occupies the same position as a judgment creditor with an execution in his hands at the time of the adjudication; the amendment in question being in the following language: * * *

"The Bankruptcy Act was intended to secure an equal and equitable distribution of the assets of the bankrupt among all creditors, * * *

"It will be seen that the provisions of the law [Maryland statute of registration] clearly require that mortgages of personal property shall be recorded within 20 days from the date thereof, and it is apparent that the real purpose of the statute is to prevent one from disposing of his property by mortgage, bill of sale, or other secret conveyances. This requirement renders it impossible

for one to execute a secret lien and thereafter deal with the public as though nothing had transpired to lessen or impair his financial ability."

In *re Bazemore*, 26 A. B. R. 494, 189 Fed. 236 (D. C. Ala.): "Before the amendment to the Bankruptcy Act, the trustee's title as against a claim under an unrecorded conditional sale, though the State law required record, did not prevail. (*Crucible Steel Co. v. Holt* (C. C. A., 6th Cir.), 23 Am. B. R. 302, 174 Fed. 127). It was to obviate this, among other things, that § 47, clause 2, subdivision a, of the Act was amended by inserting the words 'And such trustees, as to all property in the custody or coming into the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies, and powers of a creditor holding a lien by legal or equitable proceedings thereon.' (Statement of Representative Shirley to the House of Representatives, Congressional Record, 61st Congress, 2d session, pp. 2552-4). And to vest in the trustee the same right to attack secret unrecorded liens, where record was required by the State law, as was given to the judgment creditors and others under that law. It seems to me that the language of the amendment should be construed to effectuate this result if it fairly admits of such construction. If the operation of the amendment is restricted to cases in which a creditor has in fact acquired a lien by legal or equitable proceedings, then it adds nothing to the law as it was under the original act. By virtue of § 67 of the original act the trustee was subrogated to such a lien, if created within four months, and could enforce it for the benefit of the estate. If created beyond four months from the filing of the petition, it was, of course, valid as against the trustee, under both the original and amended acts. The class of cases, unprovided for by the original act, and intended to be reached by the amendment, was that in which no creditors had acquired liens by legal or equitable proceedings and to vest in the trustee for the interest of all creditors the potential rights of creditors potential with such liens. The language is readily susceptible of this construction. It recites that such trustee 'shall be deemed vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon.' This language aptly refers to such rights, remedies and powers as a creditor holding such a lien is entitled to under the law, rather than to the rights, remedies and powers of a creditor who had actually fastened a lien on the property of the bankrupt estate."

In *re Nelson*, 27 A. B. R. 272, 191 Fed. 233 (D. C. S. Dak.): "Under § 47, subdivision (a) (2) of the Bankruptcy Act, as amended in 1910, if property coming into the custody of the court be claimed by another, the trustee is vested with all the rights, remedies, and powers of a creditor holding a lien by legal or equitable proceedings thereon. Applying its plain interpretation to this section and amendment, it follows that an agreement which would have been binding upon and could have been enforced between the parties hereto prior to the Amendment of 1910 no longer necessarily binds the trustee. His position is no longer the same as that of the bankrupt, but he is now in the position of a creditor holding a legal or equitable lien, and in this case the conditional sale of this property and the writing above set forth, termed a 'warehouse receipt,' are to be interpreted exactly as if the trustee were a creditor holding such lien."

Bank of North America v. Pennsylvania Motor Car Company, 235 Pa. 194: "The manifest purpose of the Amendment was to enlarge the rights, remedies and powers of the trustee in bankruptcy, and it had the effect of vesting in the trustee, the rights, remedies and powers of a judgment creditor having a lien. In other words the trustee * * * was given every right which a creditor would have had."

In *re Smith*, 29 A. B. R. 527, 198 Fed. 876 (D. C. Wis.): "Prior to the pas-

sage of this amendment, a trustee in bankruptcy was vested with no better right or title to the bankrupt's property than belonged to the bankrupt at the time when the trustee's title accrued. He 'stood in the shoes of the bankrupt,' and had no greater right; and where, under the State law, which was binding on the bankruptcy court, a chattel mortgage was valid as between the bankrupt and the mortgagee, but not against purchasers, mortgagees or creditors, it was good as against a trustee in bankruptcy. The adjudication of bankruptcy was not an assertion of a lien, and did not put the trustee in the position of creditors who had, through process, acquired specific liens against the property covered by the mortgage. In other words, if the mortgage, though not filed, was good between the parties, the trustee was not a purchaser, a mortgagee, nor a lienee."

In *re Dancy, etc., Co.*, 28 A. B. R. 444, 198 Fed. 336 (D. C. Ala.): "One of the purposes of the amendment was to confer on trustees in bankruptcy the same right to avoid secret unrecorded liens as the creditors would have had under the State laws had not the bankruptcy intervened and the exercise of which they are deprived of by the bankruptcy proceeding. The rights of creditors to avoid unrecorded liens, which the Bankruptcy Act confers on trustees, are to be determined by the laws of the particular State requiring the record. The act was intended to give to the trustee the rights, remedies and powers of each and all classes of creditors who are clothed by the recording statutes of the States, as construed by their courts, with the right to avoid such secret and unrecorded liens or conveyances."

In *re Franklin Lumber Co.*, 26 A. B. R. 37, 187 Fed. 281 (D. C. Pa.): "It is to be noted that § 47a (2) as amended by the Act of June 25, 1910, applies to the present dispute. Under that amendment, if property coming into the custody of the court be claimed by another, the trustee is vested with all the rights, remedies, and powers of a creditor holding a lien by legal or equitable proceedings thereon. An agreement therefore which would previously have been valid between the parties—such, for example, as was considered in *Davis v. Crompton* (C. C. A., 3d Cir.), 20 Am. B. R. 53, 158 Fed. 735 (209 U. S. 548)—is no longer necessarily valid against the trustee. * * *

"Assuming that the bankrupt would be bound by the words of this agreement and could not deny it to be a lease, his trustee is not so bound, and may contend that the contract is really one of conditional sale. In such a contention he may offer any competent and relevant evidence, and it is obvious I think that the conduct of the parties may ordinarily throw much light on the true meaning of their agreement. If they treat it as a contract of sale, it makes no difference what name they have given it. A creditor may adopt his own construction, and they cannot successfully object. This is well settled in Pennsylvania and elsewhere. *Brunswick v. Hoover*, 95 Pa. 508; *Peek v. Hein*, 127 Pa. 500; *Ott v. Sweatnam*, 166 Pa. 217." This case further quoted at § 1228.

Obiter, In *re Geiver*, 28 A. B. R. 413, 193 Fed. 128 (D. C. S. Dak.): "* * * under section 47 subd. 'a.,' clause 2, as amended by the Act of June 25th, 1910, this property having come into the custody of the court and being claimed by the Henderson State Bank, the trustee is vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon.

"It follows that these chattel mortgages which would have been binding upon, and could have been enforced between the parties hereto, prior to the Amendment of 1910, no longer necessarily bind the trustee. His position is no longer the same as that of the bankrupt, but he is now in the position of a creditor holding a legal or equitable lien, and in the case at bar the chattel mortgages are to be interpreted exactly as if the trustee was a creditor holding such lien." However, whilst the foregoing correctly enunciates the law yet it was obiter, because,

even *before* the Amendment of 1910, fraudulent transfers or holdings were voidable by the trustee, see post, § 1209, and this case was that of a chattel mortgage with power of sale, void for fraud under State law, in any event."

Thus, the trustee is vested with the rights of judgment creditors.⁸⁹

Thus, an unrecorded chattel mortgage, or unrecorded conditional sales contract is void as against the trustee.⁹⁰

Thus, dower right is cut off where by the state law dower is not good against a levying creditor, or, as in Pennsylvania, where the wife has dower only in what remains after payment of debts.⁹¹

Thus, the trustee is entitled to the same rights which an execution creditor would have if property in the custody of the bankrupt had been seized by an officer under a writ of attachment or execution; or, where the property consists of money which has been deposited in a bank, if garnishment proceedings had been instituted and served on the depository.⁹²

Thus, the trustee is a creditor armed with process as to a rescission of sale for the fraud of the bankrupt, and his rights are subordinate to those of the defrauded seller where the State law subordinates the rights of an execution creditor to a defrauded seller.⁹³

On the other hand the trustee gets no more rights than creditors "armed with process" under State law. It is also to be borne in mind, that so far as the Amendment of 1910 is concerned, it simply makes available to the trustee the rights conferred by State law upon creditors "armed with process" and the trustee gets no more than such rights.

Thus, where under State law a levying creditor would take subject to an "equitable lien" on after-acquired property, likewise the trustee would take subject thereto and adopt the local construction of the law.^{93a}

Amendment of 1910 Adopts Formerly "Rejected Doctrine."—By the Amendment of 1910 to the Bankruptcy Act, § 47a (2), the formerly "rejected doctrine" that bankruptcy operates as an "equitable levy" as to property in the custody of the bankruptcy court—has become the accepted doctrine.⁹⁴

89. In re Calhoun Supply Co., 26 A. B. R. 528, 189 Fed. 537 (D. C. Ala.).

90. Milliken v. Second Nat'l Bank of Balt., 30 A. B. R. 477, 206 Fed. 14 (C. C. A. Md., reversing 29 A. B. R. 613), quoted supra; In re Farmer's Co.-Op. Co., 30 A. B. R. 187, 190, 202 Fed. 1005 (D. C. N. D.), quoted supra, and at § 1225¾.

91. In re Codori, 30 A. B. R. 453, 207 Fed. 784 (D. C. Pa.), quoted at § 1164¼; Matter of Wolf Freedman, 31 A. B. R. 53, — Fed. — (D. C. Pa.).

92. In re M. E. Dunn & Co., 28 A. B. R. 127, 193 Fed. 212 (D. C. Ark.).

93. In re Gold, 31 A. B. R. 18, — Fed. — (C. C. A. Ills.).

93a. In re Flatlands, 28 A. B. R. 476, 196 Fed. 310 (C. C. A. Wash.).

94. Before the Amendment of 1910 to § 47 (a) (2) the title of the trustee so far as it was in excess of the bankrupt's title as explained in the text, was much more restricted than now. The following was a correct statement of his then-limited title and rights as successor to creditors.

In cases affected by the fraud of the bankrupt towards creditors, the trustee was vested with the title to and could recover the property involved, and in cases where there had

See Report No. 691 of the Senate Judiciary Committee of the 61st Congress, Second Session stating the law as it existed before the Amendments of 1910, "One of the most important decisions under the present law is *York Manufacturing Company v. Cassell* (201 U. S. 344), wherein it was held that property

been some transfer or encumbrance of the property, void as to creditors by state law for want of record or otherwise, the trustee was held to succeed, and to succeed merely to the rights of any creditor who was actually then qualified under the state law to avoid the transfer or encumbrance or to take advantage of the fraud; in addition to which he possessed the peculiar rights and title conferred by the Bankruptcy Act to avoid preferences, and liens by legal proceedings acquired within four months of the filing of the bankruptcy petition.

But the Creditor's Title Taken by the Trustee, Formerly, Was That Only of Some Existing Creditor "Armed with Process."—The statute did not, before the Amendment of 1910, by its wording specify what was meant by the use of the word "creditor" in this connection, although in its § 1 of definitions, the word "creditor" was defined to mean anyone holding a debt, claim or demand provable in bankruptcy. Moreover, the phraseology of § 70 (e), giving the trustee the right to avoid any transfer made by the bankrupt which any creditor "might" have avoided, would not necessarily seem to have implied that some creditor must actually, before the time of the filing of the bankruptcy petition, already have taken all the formal steps, such as the obtaining of judgment against the bankrupt or the attaching of the bankrupt's property before judgment, required of creditors in the process of subjecting debtors' property; and such was the holding in some cases, even before the Amendment of 1910.

Beasley v. Coggins, 12 A. B. R. 355, 57 So. Rep. 213: "A trustee in bankruptcy occupies a relation similar to that of a judgment creditor of the bankrupt, and may file a bill in equity to set aside a fraudulent conveyance of real estate by the bankrupt, although neither the trustee nor any creditor has reduced any claim against the bankrupt to judgment."

The statute seemed, even before the Amendment of 1910 to strive to give to the trustee the same rights and remedies that any creditor "might" have exercised to avoid transfers, whether actually exercised or not, and such provision might not unnaturally have been construed to give him either the

right to take all the necessary steps that would have been required of such creditor, or, perhaps, even to have dispensed with such preliminary steps altogether. Certainly, since the pendency of the bankruptcy proceedings itself ties the creditors' hands from helping themselves by their ordinary remedies, it might have seemed not only a natural but also an eminently equitable construction of the law even before the Amendment of 1910 to have held that the trustee was subrogated not only to all rights and remedies for avoiding transfers which any creditor had already begun to assert, but also to all rights and remedies which any creditor "might" have asserted, as, indeed, the very wording of § 70 (3) appears to indicate. Impliedly *In re Shaw*, 17 A. B. R. 205 (D. C. Me.).

Furthermore, it is a familiar rule in the subject of the equitable remedies of creditors that where there is already a sequestration of all the debtor's property for the benefit of creditors, the obtaining of a preliminary judgment against the debtor, and the return of execution unsatisfied, being vain things, will not be required before resort may be had to equitable remedies against transferees of such debtor and other parties obligated to creditors by virtue of the debtor's dealings with them while insolvent; and this rule was held in some cases applicable in bankruptcy, even before the Amendment of 1910 "armed" the trustee "with process."

Mueller v. Bruss, 8 A. B. R. 442, 112 Wis. 406: "There can be no doubt about the general proposition that, before a mere creditor or his representative can attack a conveyance alleged to have been made by his debtor in fraud of his creditors, he must show that he has exhausted his legal remedies. * * * Obtaining judgment on the claim with a return of an execution unsatisfied, is prima facie evidence of the exhaustion of all legal remedies against the debtor. The rule stated, however, is not inexorable and without exceptions. If it appears that for any reason a judgment against a debtor can not be obtained, it will be excused as a preliminary to a creditor's suit. * * * The principle involved in the exceptions to the rule is that

covered by an unrecorded instrument, which would have been void in the State courts had the property been taken by an assignee or receiver or levied upon by attachment or execution, was not void where possession was taken by a receiver or trustee in bankruptcy, the Supreme Court holding that the trustee stood precisely in the bankrupt's shoes with regard to the unrecorded

when a party has done all that is possible for him to do to prepare his case for equitable cognizance, he is not to be denied access to the only tribunal capable of granting relief."

Skilton v. Codington, 15 A. B. R. 817, 185 N. Y. 80: "The rule that a creditor must first recover a judgment is simply one of procedure and does not affect the right. Therefore, where the recovery of a judgment becomes impracticable, it is not an indispensable requisite to enforcing the rights of the creditor." See, also, *In re Bement* (*Smith v. Mishawaka Woolen Mfg. Co.*), 22 A. B. R. 616, 172 Fed. 98 (C. C. A. Wis.).

Also, Bankr. Act, § 67 (a), providing that "claims which for want of record, or for other reasons, would not have been valid liens as against the claims of the creditors of the bankrupt, shall not be liens against his estate," and Bankr. Act, § 67 (b), providing that "whenever a creditor is prevented from enforcing his rights as against a lien created or attempted to be created by his debtor who afterwards becomes a bankrupt, the trustee of the estate of such bankrupt shall be subrogated to and may enforce such rights of such creditor for the benefit of the estate," are strongly indicative of such intention.

Crucible Steel Co. v. Holt, 23 A. B. R. 302, 174 Fed. 127 (C. C. A. Ky.): "That decision necessarily negatives the application to such a case of the provision of act July 1, 1898, § 67a, that, 'claims which for want of record, or for other reasons, would not have been valid liens as against the claims of the creditors of the bankrupt, shall not be liens against his estate,' and the further provision of § 67b, that 'whenever a creditor is prevented from enforcing his rights as against a lien created or attempted to be created by his debtor who afterwards becomes a bankrupt, the trustee of the estate of such bankrupt shall be subrogated to and may enforce such rights of such creditor for the benefit of the estate.' Those provisions were not referred to in the opinion of the court and, of course, their meaning and scope were not defined further than is done by the necessary implication from the decision; but it cannot be supposed they were overlooked."

See *Sheldon v. Parker*, 11 A. B. R. 169 (Neb. Sup. Ct.). Compare, to same effect, *In re Falls City Shirt Mfg. Co.*, 3 A. B. R. 437, 98 Fed. 592 (D. C. Ky.), where the court held that the bankruptcy absolves the lienors under a mechanics' lien statute from the requirement of the institution of legal proceedings within a certain specified time.

In re Standard Tel. v. Elec. Co. [*Knapp v. Milw T. Co.*], 24 A. B. R. 761, 216 U. S. 545 (affirming 20 A. B. R. 671, 162 Fed. 675, 19 A. B. R. 491, 157 Fed. 106), quoted supra.

Such might have been an available construction of the statute as to the title of the trustee in bankruptcy, even before the Amendment of 1910 to Bankr. Act § 47 (a) (2); yet the Supreme Court did not adopt it. On the contrary the Supreme Court carried into the construction of this Act the underlying idea of all our former bankruptcy acts, as well as that of the English Bankruptcy Acts (see *Winsor v. McClellan*, 2 Story 492, Fed. Cas. 17,887) and of the Massachusetts Insolvency laws (see *In re Littlefield*, 19 A. B. R. 18, 155 Fed. 838, U. S. C. C. A. Mass.), and denied to the trustee in bankruptcy any right creditors merely might have exercised, but had not already actually exercised, or placed themselves in position under State law to exercise; the idea being that the bankruptcy adjudication in no wise in and of itself affected the title but merely transferred whatever rights the bankrupt or any of his creditors actually had acquired at the time—save and except always as to preferences and liens by legal proceedings within the four months period.

Compare, *In re Mullen*, 4 A. B. R. 227, 101 Fed. 413 (D. C. Mass.): "Probably § 70 (a) was not so much intended to avoid certain classes of transfers as to declare the right of the trustee to avoid transfers voidable by other persons. A similar observation is applicable to § 70 (a), subd. (5)."

Compare, inferentially, *Thomas v. Woods*, 23 A. B. R. 132, 173 Fed. 585 (C. C. A. Kans.).

"Creditor" Same as in State Law, So Far as Concerns Necessity of "Arming with Process."—The word

instrument, even though in the State courts had the seizure been made by an assignee in insolvency or receiver, or by the sheriff under execution or attachment, the unrecorded lien would have been void as against creditors. By this ruling the trustee in bankruptcy is held to be vested solely with the bankrupt's own ti-

"creditor" as used in the sections of the Bankruptcy Act relating to the title and rights of the trustee has the same meaning that is attached to it by the state law. [First Nat'l Bank v. Title & Trust Co., 24 A. B. R. 330, 178 Fed. 187 C. C. A. Pa., quoted at § 1228] and refers to a creditor "armed with process," where by the state law it is only as to such creditors that the inhibited transfer of the property or lien upon it is void. [Instance, Rock Island Plow Co. v. Reardon, 27 A. B. R. 492, 222 U. S. 354, affirming 22 A. B. R. 26.]

Thus, since the word "creditor," as used in this connection in statutes, generally refers to such creditors only as have levied execution or attachment, or otherwise fastened upon the property itself, an unfiled chattel mortgage or other encumbrance required by law to be filed in order to be valid as against creditors, was, before the Amendment of 1910 to Bankr. Act § 47 (a) (2) had given the trustee the rights of a creditor "armed with process," nevertheless good in bankruptcy, unless some creditor had actually levied execution or attachment, or otherwise fastened on the property before bankruptcy, and the lien of the levy had been preserved for the benefit of the estate.

York Mfg. Co. v. Cassell, 15 A. B. R. 633, 201 U. S. 344: "We have not been referred to any decision of the Supreme Court of Ohio as to the meaning of the statute requiring the filing of contracts of conditional sales, but we concur with the Circuit Court of Appeals in this case, that the statute would render the unfiled contract void as to the same class of creditors mentioned in the chattel mortgage statute. Therefore the contract would be void as to creditors who before its filing had 'fastened upon the property' by some specific liens. As to creditors who had no such liens, being general creditors only, the statute does not avoid the sale, which is good between the parties to the contract."

For discussion and reaffirmance of York case before Amendment of 1910 see (Security) Warehousing Co. v. Hand, 19 A. B. R. 291, 206 U. S. 415; In re Littlefield, 19 A. B. R. 18, 155 Fed. 838; Davis v. Crompton, 20 A. B. R. 53, 59, 158 Fed. 735 (C. C. A.

Pa.); In re Grainger, 20 A. B. R. 166, 160 Fed. 69 (C. C. A. Calif.); Bryant v. Swafford Bros., 22 A. B. R. 111, 214 U. S. 279; Crucible Steel Co. v. Holt, 23 A. B. R. 302, 174 Fed. 127 (C. C. A. Ky.); also, In re Atlanta News Pub. Co., 20 A. B. R. 193, 160 Fed. 519 (D. C. Ga.); Mishawaka Woolen Mfg. Co. v. Smith, 20 A. B. R. 317, 158 Fed. 885 (D. C. Wis.), modified, however in In re Bement (Smith v. Mishawaka), 22 A. B. R. 616, 172 Fed. 98; In re Barker, 20 A. B. R. 674 (Ref. Colo.); In re Perkins, 19 A. B. R. 134, 155 Fed. 237 (D. C. Me.); In re Pierce, 19 A. B. R. 662, 157 Fed. 755 (C. C. A. N. Dak.); Pridmore v. Puffer Mfg. Co., 20 A. B. R. 851, 163 Fed. 496 (C. C. A. S. Car.); Corbitt Buggy Co. v. Ricand, 22 A. B. R. 316, 169 Fed. 935 (C. C. A. N. Car.). Also following York v. Cassell, see Matthey v. Wolfe, 23 A. B. R. 673, 175 Fed. 619 (D. C. Neb.); York Mfg. Co. v. Brewster, 23 A. B. R. 474 (C. C. A. Tex.).

In re Standard Tel. Co., 19 A. B. R. 491, 157 Fed. 106 (D. C. Wis.), affirmed sub nom. Knapp v. Milw. Tr. Co., 20 A. B. R. 671, 162 Fed. 675 (C. C. A.); In re Hickerson, 20 A. B. R. 682, 162 Fed. 345 (D. C. Idaho); In re Newton (Swafford Bros. Dry Goods Co. v. Bryant), 18 A. B. R. 567, 153 Fed. 841 (C. C. A. Ark.); In re Youngstom, 18 A. B. R. 572, 580, 153 Fed. 97 (C. C. A. Colo.); In re Doran, 18 A. B. R. 760, 154 Fed. 467 (C. C. A. Ky.); In re Trunk Co., 23 A. B. R. 914, 176 Fed. 1007 (D. C. Pa.); In re McDonald, 21 A. B. R. 358 (Ref. Mass.); In re Gebbie Co., 21 A. B. R. 694, 167 Fed. 609 (D. C. Pa.); Fourth St. Nat. Bank v. Milbourne Mills Co., 22 A. B. R. 442, 172 Fed. 177 (C. C. A. Pa.); In re McDonald, 23 A. B. R. 51, 173 Fed. 99 (D. C. Mass.); In re Penny & Anderson, 23 A. B. R. 115 (Ref. N. Y.); In re Bement (Smith v. Mishawaka Woolen Mfg. Co.), 22 A. B. R. 616, 172 Fed. 98 (D. C. A. Wis.).

For discussion and distinction of the York v. Cassell case, see In re Standard Tel. & Elec. Co. (Knapp v. Milw. Tr. Co.), 24 A. B. R. 761, 216 U. S. 545.

In re Economical Printing Co., 6 A. B. R. 615, 110 Fed. 514 (C. C. A. N. Y.): "It remains to consider

tle, except as to property fraudulently transferred and as to property which (within four months before the bankruptcy) has been seized by a creditor by legal process or voluntarily transferred to him by way of a preference. The trustee, under the present law, does not (except as to fraudulently transferred

whether the trustee can take advantage of the non-compliance with the statute. It has always been held by the courts of New York that only such creditors can take advantage of it as are armed with some legal process authorizing the seizure of the mortgaged property, and are thereby in a position to enforce a lien upon it, * * * and that the mortgage is good as to creditors at large as well as between the parties. Under the Bankruptcy Act of 1867 (14 Stat. 517), a failure to file a mortgage of goods and chattels in the manner prescribed by law of the State, while rendering the mortgage void as against the creditors of the mortgagor if it was not accompanied by an immediate delivery and followed by an actual and continuous possession of the chattels, did not affect its validity as against the assignee of the mortgagor in bankruptcy. The assignee succeeded merely to the title of the mortgagor, and as between the mortgagor and the mortgagee the validity of the mortgage was unaffected by the failure. *Stewart v. Platt*, 101 U. S. 731, 25 L. Ed. 816. Under the present act, however, by § 67, 'claims which for want of record or for other reasons would not have been valid liens as against the creditors of the bankrupt' are not liens against his estate (subdivision 'a'), and by subdivision 'b,' whenever a creditor is 'prevented from enforcing his rights against a lien created or attempted to be created by his debtor, who afterwards becomes a bankrupt,' the trustee of the estate is subrogated to and may enforce the rights of such creditor for the benefit of the estate. And by § 70 (subd. 'e') 'the trustee may avoid any transfer by the bankrupt of his property which any creditor of such bankrupt might have avoided.' When the mortgagor was adjudicated a bankrupt, there was, so far as appears, but one judgment creditor. Whether any other creditor could have eventually entitled himself to the benefit of the statute was a matter of mere conjecture. It would have depended not only upon his own vigilance in pursuing his legal rights, but also upon the volition of the mortgagor. The mortgagor could have made a general assignment of

its property for the benefit of its creditors, or surrendered possession of the mortgaged property to the mortgagee; and in either event the right of all creditors to impeach the lien would have been extinguished. * * *

"The Bankrupt Act does not vest the trustee with any better right or title to the bankrupt's property than belongs to the bankrupt or to his creditors at the time when the trustee's title accrues. The present act, like all preceding bankrupt acts, contemplates that a lien good at that time as against the debtor and as against all of his creditors shall remain undisturbed. If it is one which has been obtained in contravention of some provision of the act, which is fraudulent as to creditors, or invalid as to creditors for want of record, it is invalid as to the trustee; and if it is one which was invalid as to some particular creditor, though valid as to other creditors, the trustee is in certain cases subrogated to the rights of that creditor. The provisions which have been quoted do not necessarily touch a lien which at the date of the adjudication of bankruptcy was valid as to the bankrupt, and could not then be disturbed by any of his creditors. The lien of the present mortgage would not have been valid as against the claims of the creditors, within the terms of subdivision 'a,' if the creditors had obtained the right to question it, but otherwise it was valid. * * *

"We conclude that, except as to the Reilly judgment, the lien of the mortgage was valid, and that the trustee is entitled only to the amount of that judgment out of the proceeds in the registry of the court."

[For discussion of the Economical Printing Co. case, see criticism in *In re Beede*, 11 A. B. R. 387, and 14 A. B. R. 708, 138 Fed. 441 (D. C. N. Y.); interpretation by same court that rendered it, *In re Garcewich*, 8 A. B. R. 151, 115 Fed. 87; held to be binding in New York, *In re Hewitt v. Berlin Machine Wks.*, 11 A. B. R. 709, 194 U. S. 302; quoted with approval, *Receiver, etc. v. Staake*, 13 A. B. R. 281, 133 Fed. 717 (C. C. A. Va.); and followed by the U. S. Supreme Court in *York Mfg. Co. v.*

property) take the rights that a creditor under State law might have acquired, but only such as some creditor has actually acquired by levy of process, and then only in the event that such levy has occurred within four months before the bankruptcy and the lien of the levy (otherwise void under § 67 f) been preserved for

Cassell, 15 A. B. R. 344; discussed in *In re Ducker*, 13 A. B. R. 760, 134 Fed. 43 (C. C. A. Ky.); also discussed in *In re Beede*, 14 A. B. R. 713, 138 Fed. 441 (D. C. N. Y.); distinguished in *In re Carpenter*, 11 A. B. R. 147, 152, 125 Fed. 831 (D. C. N. Y.).]

[The case *In re Economical Printing Co.*, held not to correctly state the law of New York in *Pontiac Buggy Co. v. Skinner*, 20 A. B. R. 206, 217 (D. C. N. Y.); *Skilton v. Codington*, 15 A. B. R. 818, 185 N. Y. 80 (N. Y. Court of Appeals); and in (*Security Warehousing Co. v. Hand*, 19 A. B. R. 291, 206 U. S. 415, quoted at § 1137; *In re Hickerson*, 20 A. B. R. 682, 162 Fed. 345 (D. C. Idaho). *In re Gerstman & Bandman*, 19 A. B. R. 145, 157 Fed. 549 (C. C. A. N. Y.): "This court in *Re Economical Printing Company*, 6 Am. B. R. 615, 110 Fed. 514, 517, held that a non-filed mortgage was void only as to creditors who by judgment or attachment or otherwise had seized or were in a position to seize the mortgaged property. Since that decision, however, the Court of Appeals of the State of New York has held that a non-filed mortgage is void as to general creditors although it can not be attacked until they are in a position to seize the mortgaged property by virtue of a judgment, attachment or otherwise. This, however, is a mere matter of procedure and the mortgage is none the less void as to them. Cullen, Ch. J., says in that case: 'As appears by the opinion the result was reached on the assumption that by the law of the State of New York a non-filed chattel mortgage was void only as to judgment creditors obtaining a lien, not as to general creditors. We think the very eminent judge who wrote in the case misconceived the law of the State in this respect. If it were a Federal question we would follow the decision regardless of our own opinion, but as the question is as to the law of this State we must adhere to the prior decisions of this court.' *Skilton v. Codington*, 185 N. Y. 80, 88, 15 Am. B. R. 810. As we are bound to follow the construction of the State law adopted by the highest court of the State, the case of the *Economical Printing Company* must be held to have gone too far in deciding

that a non-filed mortgage is valid as to general creditors. Regarding the mortgage as void, though not subject to attack because there were no judgments against the bankrupts at the time of the adjudication, the question is whether the trustee is in a position to attack it. We think he is." Citing §§ 67 (a) (d), 70 (a), 70 (a) (5).]

Where "Arming with Process" Not Requisite by State Law, Not Requisite in Bankruptcy.—And where "arming with process" is not necessary by the state law, it was held, even before the Amendment of 1910, not to be requisite in bankruptcy, and if by state law the lien would be void, though no creditor "armed with process" existed, it would be likewise void in bankruptcy.

Bradley, Alders & Co. v. McAfee, 17 A. B. R. 499 (D. C. Mo.): "Under the Missouri Statute it is not necessary, as under the Ohio statute, followed by the Supreme Court in *York Manufacturing Co. v. Cassell*, 201 U. S. 351, 15 Am. B. R. 633, that to enable the trustee to avail himself of the statute the creditors should, by levy or attachment anterior to the proceedings in bankruptcy, have taken steps 'to fasten upon the property for payment of the debt.' Nor does the case of *Hewitt v. Berlin Machine Works*, 194 U. S. 296, 11 Am. B. R. 709, apply, as that case arose under the New York statute, which avoided the sale only as to 'Subsequent purchasers in good faith,' and there was no evidence in the case of the creditors being such purchasers.

"As applied to the Missouri statute, the holding by the Court of Appeals of this Circuit in *In re Pekin Plow Co.*, 7 Am. B. R. 369, 112 Fed. 308, 310, is conclusive on this court, which is that:

"The institution of proceedings in bankruptcy amounts to an effectual sequestration for the benefit of all his creditors of all property of all bankrupt. By such a proceeding the creditors 'are using the courts of law and their processes for the collection of their debts,' and the creditors thereby make an effectual seizure of the property of the bankrupt."

And where the instrument was held

the benefit of the trustee by order of court. In this way a distinct advantage is given in bankruptcy to the holders of unrecorded liens. The creditors' hands meanwhile are tied from making any levy, because the separate rights of the creditors have become vested in the trustee for all; besides which, as to prop-

erty by State law to be void as to the subsequent creditors but not as to prior creditors, the principle of the *York v. Cassell* case was held not to apply, even before the Amendment of 1910, since the contest then became one between creditors under Bankr. Act, § 64 (b) (5). In *re Doran*, 17 A. B. R. 799 (D. C. Ky.); but compare, In *re Doran*, 18 A. B. R. 760, 154 Fed. 467 (C. C. A. Ky.).

Discussion of Certain Formerly Rejected Doctrines—First Rejected Doctrine—That Trustee's Title as to Property Not in Custody, Analogous to Receiver's or Assignee's in State Courts.—The doctrine was held in some cases, even before the Amendment of 1910 that, as to property not in the custody of the bankruptcy court, the effect of the bankruptcy was to give the trustee whatever rights a receiver or assignee or similar officer acting in equity for the benefit of creditors would have had in the particular State as to property not in his possession; thus, if, by the State law, preliminary judgment against the bankrupt or prior actual levy upon the property involved were necessary, that such judgment or levy would likewise be necessary in case the trustee in bankruptcy seeks to avoid a transfer; and on the other hand, if in such State such prerequisites were dispensed with in cases of similar equitable sequestrations of the debtor's property, that they would be dispensed with in suits by the trustee in bankruptcy. Compare, In *re Standard Tel. Co.*, 19 A. B. R. 491, 157 Fed. 106 (D. C. Wis.), affirmed sub nom. *Knapp v. Milwaukee Trust Co.*, 20 A. B. R. 671, 162 Fed. 675 (C. C. A., affirmed sub nom. In *re Standard Tel. & Elec. Co.* [*Knapp v. Milw. Tr. Co.*], 24 A. B. R. 761, 216 U. S. 545): "The only impediment in the way of the simple creditor is that under the rules of practice he cannot attack the mortgage by an independent action in equity. The Supreme Court of Wisconsin has, however, several times held that such a contest may be waged by an assignee representing general creditors under the said assignment laws, upon the theory that his powers were substantially the same as a trustee in bankruptcy, or a sheriff armed with an

execution. *Batten v. Smith*, 62 Wis. 92, 98, 22 N. W. 342; *Sheldon Co. v. Mayers*, 81 Wis. 627, 51 N. W. 1082; *Valley Lumber Co. v. Hogan*, 85 Wis. 366, 55 N. W. 415; *Re Ellis*, 97 Wis. 92, 72 N. W. 387. Formerly the assignee under the voluntary assignment statute represented the assignor only, but by chapter 207, p. 255, Laws 1901, he is authorized to represent creditors, and may sue to set aside any fraudulent conveyance where the creditors might have proceeded if no assignment had been made. This is in substance and effect the same authority with which the trustee is clothed under §§ 60b and 70e and other provisions of the present Bankruptcy Act. * * * It is also true that the effect of the filing of a petition in bankruptcy, as laid down in *Mueller v. Nugent*, 184 U. S. 1, 7 Am. B. R. 224, * * * has been modified by the Supreme Court in *York Manufacturing Co. v. Cassell*, 201 U. S. 344, 15 Am. B. R. 633, * * * so that the institution of bankruptcy proceedings no longer has the effect of an attachment or an injunction; but the Supreme Court of Wisconsin has squarely decided in *Mueller v. Bruss*, 8 Am. B. R. 442, 112 Wis. 406, 410, * * * that a trustee in bankruptcy under the present Act, representing only creditors at large, may maintain an action in equity to set aside transfers of property by the bankrupt in fraud of creditors. This is put upon the ground that the Bankruptcy Act renders it practically impossible for creditors to comply with the equitable rule, and that equity does not demand impossibilities. *Jackman v. Bank*, 125 Wis. 476. * * * Thus it appears that the general doctrine of equity that to institute such a suit a creditor must be armed with a judgment and execution is observed in Wisconsin, but that such rule is one of procedure only, and not a condition precedent. The same doctrine is held in *Skilton v. Codington*, 15 Am. B. R. 810, 185 N. Y. 80, 77 N. E. 790, 113 Am. St. Rep. 885. This authority is the more persuasive because Wisconsin borrowed its statute from New York. The Wisconsin law in favor of simple creditors commends itself to me on stronger grounds than mere comity. It is in

erty already in the custody of the bankruptcy court, of course individual creditors would be in contempt of court should they levy thereon. Thus the evil of secret liens has continued. It is this evil and the injustice worked upon creditors who rely upon the debtors' apparent ownership against which the bankruptcy

harmony with the spirit of the bankrupt law."

Second Formerly Rejected Doctrine—That Bankruptcy Operates as "Equitable Levy," as to Property in Custody.—The second formerly rejected doctrine was that bankruptcy itself operated as an equitable levy as to property in the custody of the bankruptcy court.

The rule that the word "creditor" as used in the Bankruptcy Act refers to the same kind of creditors meant by the State statutes in avoiding transfers and liens—i. e., in general, to creditors "armed with process"—was perfectly consistent, to be sure, with the theory that, as to property in the custody of the bankruptcy court itself, i. e., property in the possession or control of the bankrupt after adjudication, or of the marshal, receiver or trustee in bankruptcy, either before or after adjudication, the bankruptcy itself operated as an equitable levy; so that, as to such property in States where equitable sequestration operated as a sufficient "arming with process," the bankruptcy itself would likewise have operated to arm with process the trustee for creditors in bankruptcy, and such was the apparent holding in many cases.

In *re Rodgers*, 11 A. B. R. 93, 125 Fed. 169 (C. C. A. Ills., reversed, on other grounds, sub nom. *Bank v. Title & Trust Co.*, 14 A. B. R. 102, 198 U. S. 280): "The filing of the petition, followed by seizure and by adjudication in bankruptcy, is a seizure of the property by the law for the benefit of creditors, and an appropriation of it to the payment of the debts of the bankrupt. It is a seizure of the property by legal process, equal in rank to and of the same force and effect as by execution or attachment."

Also, In *re Nat'l Bk.*, 14 A. B. R. 184, 135 Fed. 62 (C. C. A. Ohio).

Bankruptcy So Operating as Equitable Levy Precisely as Other Equitable Levies Operate in Same State.—It was a corollary of the formerly rejected doctrine, however, that the bankruptcy operated as such equitable levy on titles in each state only as other equitable levies there operated. While, in accordance with the formerly rejected doctrine under consid-

eration it would be true that bankruptcy, being beyond question a proceeding in equity, would have operated upon titles in each State as other equitable proceedings would have operated there, it correspondingly would have been true that its operation in each State would have been limited to that of similar equitable proceedings in such State. Thus, if, under State law, it required some particular method of seizure by legal proceedings to nullify the particular lien or transfer involved, as by execution or attachment, and if any other method of sequestration by legal proceedings, as receivership, etc., was insufficient to such end, the first-named method alone would have been effective in bankruptcy. [Impliedly, In *re Beede*, 14 A. B. R. 702, 138 Fed. 441 (D. C. N. Y.).

Formerly Accepted Doctrine—Bankruptcy Not an Equitable Levy.

—The doctrine adopted, however, was different; and bankruptcy was held not to be in the nature of an equitable levy, whether the property were in the actual custody of the bankruptcy court or not. The bankruptcy proceedings, though equitable, were not, in this respect, held to be analogous to a creditor's bill, but on the contrary were held to effect no change in and of themselves, but merely to give the trustee whatever rights the bankrupt and his creditors at the time of bankruptcy actually possessed under state law and were capable of asserting thereunder (save and except always as to the peculiar rights conferred by the Bankruptcy Act, upon bankruptcy, to avoid preferences and liens obtained by legal proceedings within the four months prior to the bankruptcy).

However much might have been said under the law as it then stood without Amendment for the formerly discarded doctrine that bankruptcy operated (as to all property, at any rate, in the custody of the bankruptcy court), precisely as other equitable sequestrations of like nature so operated under the state law, yet such doctrine was expressly and emphatically repudiated by the Supreme Court of the United States; and the contrary doctrine was adopted, namely, that bankruptcy did not operate as

law has set its face. The proposed amendment, whilst correcting the defect named, at the same time carefully guards the rights of all parties. It is evident that in the proposed amendment attempt is made to give effect to two ideas quite distinct: First, that as to the property in the custody of the bankruptcy court the bankruptcy trustee shall be considered to have the same title that a creditor holding an execution or other lien by legal or equitable proceedings levied upon that property would have under State law; and, second, that as to property not in the custody of the bankruptcy court the trustee should stand in the position of a judgment creditor holding an execution returned unsatisfied, thus entitling him to proceed precisely as an individual creditor might have done to subject assets. In this way, in effect, proceedings in bankruptcy will give to creditors all the rights that creditors under the State law might have had had there been no bankruptcy and from which they are debarred by the bankruptcy—certainly a very desirable and eminently fair position to be granted to the trustee."

In *re Farmers' Supply Co.*, 28 A. B. R. 535, 196 Fed. 990 (D. C. Ga.): "This amendment made a vital change in the act. Instead of the trustee having no greater right than the bankrupt would have, he now has, and had when the pres-

would an equitable levy under State laws, even as to property in the actual custody of the bankruptcy court, and that bankruptcy proceedings were not to be considered to be analogous to creditors' bills in this respect.

York Mfg. Co. v. Cassell, 15 A. B. R. 635, 201 U. S. 344: "We come then to the question whether the adjudication in bankruptcy was equivalent to a judgment, attachment or other specific lien upon the machinery. The Circuit Court of Appeals has held herein that the seizure by the court of bankruptcy operated as an attachment and an injunction for the benefit of all persons having interests in the bankrupt's estate.

"We are of opinion that it did not operate as a lien upon the machinery as against the York Manufacturing Company, the vendor thereof. Under the provisions of the Bankrupt Act the trustee in bankruptcy is vested with no better right or title to the bankrupt's property than belonged to the bankrupt at the time when the trustee's title accrued. At that time the right, as between the bankrupt and the York Manufacturing Company, was in the latter company to take the machinery on account of default in the payment therefor. The trustee under such circumstances stands simply in the shoes of the bankrupt and as between them he has no greater right than the bankrupt. This is held in *Hewitt v. Berlin Machine Works*, 194 U. S. 296, 11 Am. B. R. 709. The same view was taken in *Thompson v. Fairbanks*, 196 U. S. 516, 13 Am. B. R. 437. It was there stated that 'under the present Bankrupt Act, the

trustee takes the property of the bankrupt, in cases unaffected by fraud, in the same plight and condition that the bankrupt himself held it, and subject to all the equities impressed upon it in the hands of the bankrupt.' See *Yeatman v. Savings Institution*, 95 U. S. 764; *Stewart v. Platt*, 101 U. S. 731; *Hauselt v. Harrison*, 105 U. S. 401. The same doctrine was reaffirmed in *Humphrey v. Tatmen*, 198 U. S. 91, 14 Am. B. R. 74. The law of Ohio says the conditional sale contract was good between the parties, although not filed. In such a case the trustee in bankruptcy takes only the rights of the bankrupt, where there are no specific liens, as already stated.

"The remark made in *Mueller v. Nugent*, 184 U. S. 1, 7 Am. B. R. 224, 'that the filing of the petition (in bankruptcy) is a caveat to all the world, and in effect and attachment and injunction,' was made in regard to the particular facts in that case. The case itself raised questions entirely foreign to the one herein arising, and did not involve any inquiry into the title of a trustee in bankruptcy as between himself and the bankrupt, under such facts as are above stated.

"In this case, under the authorities already cited, the York Manufacturing Company had the right, as between itself and the trustee in bankruptcy, to take the property under the unfiled contract with the bankrupt, and the adjudication in bankruptcy did not operate as a lien upon this machinery in favor of the trustee as against the York Manufacturing Company."

ent bankruptcy proceeding was instituted, the 'rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings.' The lien or priority would undoubtedly be superior to that of the creditor selling goods by a conditional bill of sale as against the property or so much thereof at might come into the hands of the trustee. * * *

"In the case of Williamsburg Knitting Mill (D. C. Va.), 27 Am. B. R. 178, 190 Fed. 871, Judge Waddill, in the District Court for the Eastern District of Virginia expresses the same view. In the opinion Judge Waddill says, quoting from 3 Remington on Bankruptcy, p. 331: 'By the Amendment of 1910 to the Bankruptcy Act, § 47a (2), this rejected doctrine that bankruptcy operates as an equitable levy as to property in the custody of the bankruptcy court, has become the accepted doctrine.' Judge Waddill continues:

"Moreover, this author shows that Congress by the amendment in question purposely sought to modify the decision of *York Manufacturing Co. v. Cassell*, 201 U. S. 344, 15 Am. B. R. 633, 26 Sup. Ct. 481, 50 L. Ed. 782. At page 231 of the same volume (3 Remington) the report of the Senate Judiciary Committee on the amendment of the act is set out in full, stating in terms that its object and purpose was to meet the decision in the *York* case, and to adopt in lieu thereof the views herein taken. *Collier on Bankruptcy* (8th ed.), pp. 541, 542, refers to this amendment approvingly, and, in effect, takes the same view on the act that Remington does, though he calls attention to the fact that more logically the amendment should have been made to section 70 of the Bankruptcy Act, instead of § 47.'"

§ 1270 1/10. Whether Amendment Retroactive—Whether Trustee Stands as "Creditor Armed with Process" as to Liens and Contracts Made before Amendment.—It was held in one case that the Amendment of 1910 to § 47a (2), wherein the trustee is given the rights of a levying creditor, is not retroactive and does not apply to liens and contracts entered into before that amendment took effect.

Arctic Ice Machine Co. v. Armstrong County Trust Co., 27 A. B. R. 562, 192 Fed. 114 (C. C. A. Pa.): "The contract before us antedates the Amendment. The rights of a vendor and vendee were fixed by it. Under the law of Pennsylvania the reservation of title in the Arctic Ice Machine Co. was from March 22, 1909, the date of the contract of sale, to June 25, 1910, the date of the amendment, against any trustee in bankruptcy that might have been appointed for Keener Bros. To hold that the amendment divested the vendor of its reserved title is, independent of any constitutional question, to give it a retroactive effect, not consistent with any expressed intent of Congress. The principle is too well established to be disregarded that a statute shall not, except where the legislative intent is clear, be permitted to have a retroactive effect."

But it has also been held that the Amendment of 1910 is purely remedial, intended to correct a misinterpretation of the Bankruptcy Act, and is not retroactive if applied to liens and contracts entered into before the amendment.

In *re Farmers' Co-Op. Co. of Barlow No. 2*, 30 A. B. R. 190, 202 Fed. 1005 (D. C. N. Dak.): "The contract of February 23, 1910, was made prior to the Act of 1910, amending § 47 of the Bankruptcy Act, and the referee for this reason held, following *Arctic Ice Mach. Co. v. Armstrong County Trust Co.* (C. C. A. 3rd. Cir.), 27 A. B. R. 562, 192 Fed. 114, 112 C. C. A. 458, that the Act of 1910 did not

apply to articles furnished under that contract, and directed the trustee to return them to the harvester company. The case cited is not a binding authority in this court, but, owing to the eminent court by which it was rendered, I feel great reluctance in taking a different view of the statute from that there adopted. The question, however, was not very fully considered, and it seems to me that the decision proceeds upon a wrong interpretation of the Act. The history of the statute, as given by Remington, vol. 3, p. 331, and explained in *Re Farmers' Supply Co.* (D. C. Ga.), 28 A. B. R. 535, 196 Fed. 991, and in *Re Williamsburg Knitting Co.* (D. V. A.), 27 A. B. R. 178, 190 Fed. 871, shows that it was purely remedial, intended to correct a misinterpretation of the Bankruptcy Act by the courts. This view is also manifest on the fact of the statute. It declares that trustees in bankruptcy 'shall be deemed' vested with the rights, remedies, etc. It therefore gives a rule of interpretation rather than a substantive right. Remedial and curative statutes may properly be given a retroactive effect. *Sutherland on Statutory Construction*, §§ 482, 483. The rule is peculiarly applicable in the present case, for the invalidity of the unfiled contract was created, not by the amendment of § 47, but by the State statute, which was in force at the time the contract was made. All the federal law does is to give effect to the invalidity already declared by the State law. It simply enables the trustee, as the representative of creditors, to assert the same rights which the creditors themselves would have possessed if bankruptcy had not intervened. Another reason for this interpretation is found in the fact that the statute is part of a Bankruptcy Act, and that Act generally applies to contracts made prior to its adoption, the same as to subsequent contracts."

And it was held in one case that a failure to properly refile a chattel mortgage after the Amendment of 1910 will vitiate the mortgage, even though the mortgage itself was executed before the amendment and that such a ruling would not be giving to the amendment a retroactive effect.⁹⁶

§ 1270 2 10. Date When Trustee's Lien or Execution Rights Arise.—The interesting question arises under the Amendment of 1910 to the Bankruptcy Act, § 47a (2), endowing the trustee with the rights of a creditor "armed with process" as to what shall be considered as the date that these rights shall be deemed to have arisen. As to property in the custody or coming into the custody of the bankruptcy court, the right of the trustee as a lien creditor must be held to be the same as that of a creditor actually levying at the time of the acquisition of the custody by the bankruptcy court, whether the trustee had been qualified or not and irrespective also of the date of the adjudication, the property so affected being bound either as of the date of such acquisition of custody, as in some States, or, in other States as of the date of the issuance of process, namely, the filing of the bankruptcy petition and issuance of the subpoena thereunder, dependent in each instance on State law. The title which the trustee, under Bankruptcy Act, § 70, acquires by operation of law is a different title from that which he acquires by operation of law under § 47a (2) of the Amendment of 1910. The title conferred upon the trustee by the

⁹⁶. In *re Smith*, 29 A. B. R. 527, 198 Fed. 876 (D. C. Wis.), quoted at § 1240.

Bankruptcy Act, § 70, is the "title of the bankrupt," and it is to date from the date of the adjudication, but the title conferred by the Amendment of 1910, under § 47a (2) is not the title of the bankrupt, nor is it a title derived by subrogation from any creditor; it is an independent title, derived neither by subrogation to the bankrupt's rights, nor by subrogation to any creditor's existing rights, but conferred upon the trustee by the statute, whereby the trustee is endowed with the attributes of a creditor "armed with process" under the State law, irrespective of the actual existence of any creditor then and there "armed" with such process. So what the statute intends to do is to give to the seizure or possession by the bankruptcy officials or bankrupt at the time of the filing of the bankruptcy petition or thereafter, whether such seizure be effected by such trustee himself, or by the marshal or a receiver, or even by the bankrupt, the effect of a levy in behalf of all creditors.

Likewise, as to property not in the custody of the bankruptcy court, the filing of the petition, followed by subsequent adjudication, is to be held analogous to the return of an execution unsatisfied, unless, later on, custody thereof is acquired, in which event such obtaining of custody will amount to a levy at law, or by equitable process such as by creditor's bill, injunction, etc.

At any rate, the trustee's rights do not antedate the filing of the bankruptcy petition.

Hart v. Emmerson-Brantingham Co., 30 A. B. R. 218, 203 Fed. 60 (D. C. Mo.): "It seems reasonably clear that the rights, remedies and powers with which the trustee is invested arise, by relation, as of the date of the commencement of the bankruptcy proceedings, or as of the date of the adjudication of bankruptcy and not as of an earlier date."

In re Farmers' Co-Op. of Barlow, 30 A. B. R. 187, 202 Fed. 1008 (D. C. N. Dak.): "This language [Bankruptcy Act, § 47a (2)] measures the right of the trustee. The history of the statute as above outlined shows that those rights are obtained by the filing of the petition in bankruptcy. That act is, by the amendment, given the same force as the seizure of the property under execution or attachment of a creditor and cannot be given any retroactive effect. The right to go back four months from the date of the filing of the petition is confined to transactions which are specifically enumerated in the Bankruptcy Act, and the courts cannot properly apply those provisions to other transactions."

On the other hand, to hold that the rights of the trustee as a creditor "armed with process" do not arise until adjudication, would largely defeat the object of the Amendment of 1910, and would afford a convenient method of perpetuating the evils sought to be remedied, by affording opportunity for recording after the nonrecording had accomplished the harm meant to be guarded against by the registration acts of the various states.⁹⁷

⁹⁷ *In re East End Mantel & Tile Co.*, 29 A. B. R. 793, 202 Fed. 275 (D. C. Pa.); *Matter of Superior Drop Forge & Mfg. Co.*, 31 A. B. R. 455, 208 Fed. 813 (D. C. Ohio); *In re*

Jacobson & Perrill, 29 A. B. R. 603, 200 Fed. 812 (D. C. Ga.); *Big Four Implement Co. et al. v. Isom Wright*, 31 A. B. R. 125, 207 Fed. 535 (C. C. A. Kans.), quoted at § 1270 3/10.

§ 1270 3/10. Conditional Sales, Chattel Mortgages, etc., Withheld from Record, but Filed Prior to Bankruptcy.—Unless there be fraud, a conditional contract of sale, or a chattel mortgage, withheld from record for a time but filed or recorded prior to the bankruptcy, is good as against the trustee, if there be no existing creditor armed with process prior to the filing or recording, since the lien given to the trustee by virtue of the Amendment of 1910 to § 47a (2), cannot be considered as arising until the bankruptcy.⁹⁸

Big Four Implement Co. et al. v. Isom Wright, 31 A. B. R. 125, 207 Fed. 535 (C. C. A. Kans.): "This amendment must speak as of the time of the bankruptcy. The lien which the trustee is considered as holding must be a lien attaching as of that date. There can be no ground for saying that the lien is in existence before the bankruptcy. No case has been cited which so holds. In most of the cases referred to by the trustee the contract was never filed. In *Rock Island Plow Company v. Reardon*, 222 U. S. 354, 27 Am. B. R. 492, 32 Sup. Ct. 164, 56 L. Ed. 231, the contract was not filed, yet the vendor had taken possession of the property covered by it before the bankruptcy. It appeared, however, in that case, that prior to that possession by the vendor another creditor had secured a lien by execution, which lien was preserved by the trustee for the benefit of the creditors. There is no authority for holding that a trustee can, in his own right, avoid such contracts as these when they have been filed before the bankruptcy. The decisions are to the contrary. *Keeble v. John Deere Plow Co.* (C. C. A., 5th Cir.), 190 Fed. 1019, 111 C. C. A. 668. Part of the opinion of the court below in this case is found in *Re Jacobson & Perrill* (D. C., Ga.), 29 Am. B. R. 603, 200 Fed. 812; *Re Farmers Co-operative Co.* (D. C., N. Dak.), 30 Am. B. R. 187, 202 Fed. 1005; *Hart v. Emmerson-Brantingham Co.* (D. C., Mo.), 30 Am. B. R. 218, 203 Fed. 60. In *Sturtivant Bank v. Schade* (C. C. A., 8th Cir.), 27 Am. B. R. 673, 195 Fed. 188, 115 C. C. A. 140, it appeared that a deed was made in 1902 and not recorded until August 8, 1906. A petition in bankruptcy was filed on October 8, 1906, and an adjudication had on October 31, 1906. The trustee came into possession of the real estate covered by the deed. The court considered that any judgment lien which the trustee was deemed to have was created subsequent to August 8, 1906. It is not necessary to determine whether, under the Amendment of 1912, the lien of the trustee attached on the filing of the petition, or on the date of the adjudication, because the filing of the papers in this case preceded both dates."

Similarly, the retaking of possession before bankruptcy of property sold to the bankrupt on conditional sale, cannot be a preference.

Hart v. Emmerson-Brantingham, 30 A. B. R. 218, 203 Fed. 60 (D. C. Mo.): "It is conceded by the defendant that, if the goods in controversy had remained in the possession of the bankrupt up to the time of the adjudication of bankruptcy, the provision of the Bankruptcy Act just quoted would have rendered its title invalid as against the trustee, for, in respect of 'property in the custody or coming into the custody of the bankruptcy court,' the amendment of 1910

⁹⁸. In *re Farmers Co-Op. Co. of Barlow No. 1*, 30 A. B. R. 187, 202 Fed. 1008 (D. C. N. Dak.), quoted at § 1270 2/10; In *re East Mantel & Tile Co.*, 29 A. B. R. 793, 202 Fed. 275 (D.

C. Pa.); In *re Superior Drop Forge & Mfg. Co.*, 31 A. B. R. 455, 208 Fed. 813 (D. C. Ohio); In *re Jacobson & Perrill*, 29 A. B. R. 603, 200 Fed. 812 (D. C. Ga.).

confers upon the trustee 'all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon.' But, as the property here in question was turned over by the bankrupt to the defendant, before the commencement of the bankruptcy proceeding, and never came into the 'custody of the bankruptcy court,' the provision of § 47, clause 2, last referred to, is rendered inapplicable to the facts in the case. The trustee is thus constrained to rely on that portion of § 44, clause 2, which provides that, as to 'property not in the custody of the bankruptcy court,' the trustee 'shall be deemed vested with all the rights, remedies and powers of a judgment creditor holding an execution duly returned unsatisfied.' It seems reasonably clear that the 'rights, remedies and powers' with which the trustee is invested arise, by relation, as of the date of the commencement of the bankruptcy proceeding, or as of the date of the adjudication of bankruptcy, and not as of an earlier date."

§ 1270 4/10. But Has Rights of Levying Creditor Only as to Property in Custody or Coming into Custody of Bankruptcy Court.

—It must not be forgotten, however, that the trustee gets the rights of a levying creditor only as to property in the custody, or coming into the custody, of the bankruptcy court. As to other property he does not have the rights of a levying creditor, though he may be subrogated, as before the Amendment of 1910, to the lien of a levying creditor who has actually levied thereon within the preceding four months.

Thus, as to goods pledged.¹

§ 1270 5/10. Not an "Innocent Purchaser," Even Since the Amendment of 1910.—The trustee is no more an innocent purchaser under the Amendment of 1910 than before that Amendment.² Thus, the right of rescission of a sale for fraud of the bankrupt's purchaser is unaffected, since it is the general law that the right of a defrauded seller is superior to that of a levying creditor though not to that of a bona fide purchaser.³

1. In re Twining, 26 A. B. R. 200, 185 Fed. 555 (D. C. Pa.), although in this case there does not appear to have been a sufficient delivery even as against the alleged pledgor to have passed title.

2. Superior Drop Forge & Mfg. Co., 31 A. B. R. 455, 208 Fed. 813 (D. C. Ohio); In re Wade, 26 A. B. R. 169, 185 Fed. 664 (D. C. Mo.).

3. Same Rule before the Amendment of 1910—Not an "Innocent Purchaser."—It is incorrect to denominate him an "innocent purchaser," or to say he stands in the shoes of an "innocent purchaser," as was said in In re Thorp, 12 A. B. R. 195 (Ref. Va., affirmed by D. C.), and in In re Booth, 3 A. B. R. 574, 98 Fed. 975 (D. C. Ore.), and as was denied in Nat'l Bk. of Chattanooga v. Rome Iron Co., 4 A. B. R. 441 (C. C. Ga.), 102 Fed. 755, and in In re Kellogg, 7

A. B. R. 275, 113 Fed. 120 (D. C. N. Y.), and in In re Hunt, 14 A. B. R. 416, 139 Fed. 283 (D. C. N. Y.): "While the statute of New York (real property law, § 241) requires the recording of a real estate mortgage as against purchasers and mortgagees in good faith and for value only, such recording is not 'required' within the meaning of § 60a of the Bankrupt Act, 1898, as amended in 1903, in order to give it validity as against the mortgagor's trustee in bankruptcy, who is not a purchaser in good faith and does not occupy the position of such purchasers."

In re Beede, 14 A. B. R. 697, 138 Fed. 441 (D. C. N. Y.); In re Hewitt v. Berlin Machine Co., 11 A. B. R. 709, 714, 194 U. S. 296; In re Dunlop, 19 A. B. R. 361, 156 Fed. 545 (C. C. A. Minn.); In re Pierce, 19 A. B. R. 662, 157 Fed. 755 (C. C. A. N.

In *re Gold*, 31 A. B. R. 18, — Fed. — (C. C. A. Ill.): "The vendors having at the earliest opportunity rescinded the sale, the title to the furs in question never passed to the bankrupt, by reason of her fraudulent representations to the vendors, therefore the trustee took no title thereto inasmuch as, under the laws of Illinois, as construed by the courts of the State, the rights of the defrauded vendor prevailed over the claims of a creditor holding a lien by legal or equitable proceedings thereon."

§ 1270 6 10. **But Is a "Third Person."**—It was held before the Amendment of 1910, indeed, that under the statutes of Georgia as to the filing of conditional sales contracts, a trustee in bankruptcy is a "third person" as to whom an unfiled conditional sale contract is void.^{3a}

It has been held, also, under the Illinois statute requiring the recording of chattel mortgages, that a trustee is a "third person."^{3b}

In *re Beckhaus*, 24 A. B. R. 380, 177 Fed. 141 (C. C. Ill.): "The term 'third person' is broad enough to include everybody outside of the immediate parties to the instrument and their privies. A simple contract creditor who has not obtained a judgment is just as much a 'third person,' is just as much a stranger to the mortgage, as is the simple contract creditor who has obtained a judgment. Both have the right to enforce payment, if that can be done. The interests of both are prejudiced if the debtor's property is covered by a fraudulent transfer. If at the time of the fraudulent transfer one creditor has obtained a judgment and the other has not, the only difference is that one has proceeded farther than the other in the enforcement of his rights and the protection of his interest. And when it is said that a fraudulent transfer is void only as to judgment creditors the expression means no more than that a creditor can not seize his debtor's property until he has obtained some process which authorizes the seizure. * * * Our examination of the Illinois cases has led us to conclude that the Illinois courts have not decided, independently of procedure and having a regard solely to rights, that simple contract creditors, irrespective of the progress they may have made in suing their debtor, are not 'third persons' within the meaning and intent of the recording statute."

§ 1270 7/10. **Unfiled Chattel Mortgages, Conditional Sales, etc.—Rights of Trustee Since Amendment of 1910.**—The rights of the trustee since the Amendment of 1910 as to unfiled chattel mortgages, conditional sales, etc., and as to other rights, are to be determined in accordance with the rules heretofore laid down, remembering, however, always, that the trustee himself now is to be regarded as a "creditor" and also as a "creditor armed with process," thus causing modifications in the decisions in

Dak.); In *re (Columbia) Fire Proof & Trim Co.*, 21 A. B. R. 714, 168 Fed. 159 (D. C. N. Y.).

Zartman, Trustee v. Nat. Bank, 216 U. S. 134, 23 A. B. R. 635: "The trustee claims that he takes the same kind of title as a bona fide purchaser for value; but the rule applicable to this and all similar cases is that the trustee takes the property of the

bankrupt, not as an innocent purchaser, but as the debtor had it at the time of the petition, subject to all valid claims, liens, and equities."

3a. In *re Burke*, 22 A. B. R. 69, 168 Fed. 994 (D. C. Ga.).

3b. Similarly, the trustee has been held to be a "person other than a party thereto." In *re McDonald*, 23 A. B. R. 51, 173 Fed. 99 (D. C. Mass.).

accordance therewith, so far as concerns the specific holding in the particular case involved.

Thus, it is to be taken into account as to subjects discussed in preceding parts of the treatise relative to the meaning of "required;"⁴ as to whether an unfiled instrument is void where filing or recording is not required by the State law;⁵ whether taking possession cures lack of record;⁶ whether a lien begins at the date of taking possession, or reverts, to be determined by State law;⁷ as to after-acquired property;⁸ filing or refileing in wrong place;⁹ or in only one place where statute requires two;¹⁰ defective execution of mortgages;¹¹ defective refileing of chattel mortgages;¹² disguised conditional sales;¹³ bills of sale as mortgages;¹⁴ equitable lien upon property already pledged and in pledgee's hands;¹⁵ other equitable liens;¹⁶ agreement to insure operating as equitable assignment;¹⁷ but liens absolutely void, void in bankruptcy;¹⁸ mechanics' and subcontractors' liens not filed till after bankruptcy;¹⁹ recording, where lien on both real and personal property;²⁰ chattel mortgages or conditional sales made in State where recording not required, but contemplating delivery where required and vice versa;²¹ other liens and contracts not requiring record;²² unrecorded real estate mortgages;²³ unrecorded sales of personalty where property still in seller's hands;²⁴ owner's lien on material left on premises by bankrupt contractor.²⁵

§ 1270 8/10. Rescission for Fraud Unaffected by Amendment of 1910, Arming Trustee with Process.—The right of rescission of a sale for fraud of the bankrupt's purchaser is unaffected by the Amendment of 1910.²⁶

§ 1270 9/10. Maxim That "Filing of Petition a Caveat, Attachment and Injunction."—The maxim is repeatedly enunciated in the decisions that the "filing of the petition in bankruptcy is a caveat to all the world and in effect an attachment and injunction."²⁷

4. See ante, § 1232.

5. See ante, 1234.

6. See ante, 1236.

7. See ante, 1237.

8. See ante, 1238.

9. See ante, 1240¼.

10. See ante, 1240½.

11. See ante, 1240¾.

12. See ante, 1240.

13. See ante, 1246.

14. See ante, 1246½.

15. See ante, 1252.

16. See ante, 1253½.

17. See ante, 1253.

18. See ante, 1254.

19. See ante, 1255.

20. See ante, 1256.

21. See ante, 1247.

22. See ante, 1250.

23. See ante, 1248.

24. See ante, § 1249.

25. See ante, § 1251.

26. In re Gold, 31 A. B. R. 18, — Fed. — (C. C. A. Ill.), quoted at § 1270.

27. In re Reynolds, 11 A. B. R. 760, 127 Fed. 760 (D. C. Mont.); Crosby v. Spear, 11 A. B. R. 615, 98 Me. 542; Mueller v. Nugent, 184 U. S. 1, 7 A. B. R. 224; In re Tweed, 12 A. B. R. 648, 131 Fed. 355 (D. C. Iowa); In re Smith & Shuck, 13 A. B. R. 103, 132 Fed. 301 (D. C. Iowa); In re Granite City Bk., 14 A. B. R. 406, 137 Fed. 818 (C. C. A. Iowa); In re Kolin, 13 A. B. R. 531, 134 Fed. 557 (C. C. A. Ills.); In re Schuster, 13 A. B. R. 760 (C. C. A. Ky.); Dolle v. Cassell, 14 A. B. R. 52, 135 Fed. 52 (C. C. A. Ohio, reversed in York

Acme Harvester Co. v. Beekman Co., 222 U. S. 300, 27 A. B. R. 262: "The filing of the petition is an assertion of jurisdiction with a view to the determination of the status of the bankrupt and a settlement and distribution of his estate. The exclusive jurisdiction of the bankruptcy court is so far *in rem* that the estate is regarded as in *custodia leges* from the filing of the petition. It is true that under § 70a of the Act of 1898 the trustee of the estate, on his appointment and qualification, is vested by operation of law with the title of the bankrupt as of the date he was adjudicated a bankrupt, but there are many provisions of the law which show its purpose to hold the property of the bankrupt intact from the time of the filing of the petition, in order that it may be administered under the law if an adjudication in bankruptcy shall follow the beginning of the proceedings. Paragraph 5, § 70a, in reciting the property which vests in the trustee, says there shall vest 'property which prior to the filing of the petition, the bankrupt could by any means transfer or which might have been levied upon and sold under judicial process against the bankrupt.' Under § 67c attachments within four months before the filing of the petition are dissolved by the adjudication in the event of the insolvency of the bankrupt, if its enforcement would work a preference. Provision is made for the prompt taking possession of the bankrupt's property, before adjudication if necessary (§ 69a). Every person is forbidden to receive any property after the filing of the petition, with intent to defeat the purposes of the act. These provisions, and others might be recited, show the policy and purpose of the Bankruptcy Act to hold the estate in the custody of the court for the benefit of creditors after the filing of the petition and until the question of adjudication is determined. To permit creditors to attach the bankrupt's property between the filing of the petition and the time of adjudication would be to encourage a race of diligence to defeat the purposes of the act and prevent the equal distribution of the estate among all creditors of the same class which

Mfg. Co. v. Cassell, 15 A. B. R. 633, 201 U. S. 344). In *re Mertens*, 14 A. B. R. 226, 134 Fed. 104-5 (D. C. N. Y.), where the court held it operated to render null and void a secured creditor's selling out of his security under the terms of the agreement of pledge, before adjudication. *State Bank v. Cox*, 16 A. B. R. 35 (C. C. A. Ills.); In *re Breslauer*, 10 A. B. R. 33, 121 Fed. 910 (D. C. N. Y.).

Obiter, In *re Krinsky Bros.*, 7 A. B. R. 535, 112 Fed. 972 (D. C. N. Y.): "Those who deal with bankrupt's property after the filing of the petition and before the final adjudication, do so at their peril." In this case, however, a restraining order had actually been entered though the parties restrained had received only verbal notice thereof. In *re Benedict*, 15 A. B. R. 238, 140 Fed. 55 (D. C. Wis.); In *re Mertens*, 15 A. B. R. 369, 144 Fed. 818 (C. C. A. N. Y.); In *re Youngstrom*, 18 A. B. R. 572, 153 Fed. 97 (C. C. A. Colo.); In *re Wilk*, 19 A. B. R. 178, 155 Fed. 943 (D. C. N. Y.).

The case In *re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.), is not contra to the author's views

as above expressed in the text, although the court apparently gives adhesion to the unlimited doctrine that "immediately upon and by virtue of the adjudication, all the property of the bankrupt wherever situate and in whosoever's possession it may be, passes into the custody of the court, and upon the appointment of a trustee vests in him," the court saying: "This is undoubtedly correct and is fully sustained by the authorities cited." The proposition is not correct and never has been correct, for property does not pass "into the custody of the court" regardless of "whosoever's possession it may be in." The facts of the case and the final decision of the court are, however, wholly in conformity with the correct view, as laid down in the text.

Where a state court, in ignorance of the fact that bankruptcy proceedings had been instituted against the attachment debtor, ordered the sale of certain property as perishable, the sale was not interfered with but the trustee was relegated to the proceeds. *Jones v. Springer*, 226 U. S. 148, 29 A. B. R. 204.

is the policy of the law. The filing of the petition asserts the jurisdiction of the Federal court, the issuing of its process brings the defendant into court, the selection of the trustee is to follow upon the adjudication, and thereupon the estate belonging to the bankrupt, held by him or for him, vests in the trustee. Pending the proceedings the law holds the property to abide the decision of the court upon the question of adjudication as effectively as if an attachment had been issued, and prevents creditors from defeating the purposes of the law by bringing separate attachment suits which would virtually amount to preferences in favor of such creditors."

Obiter, *In re Zotti*, 26 A. B. R. 234, 186 Fed. 84 (C. C. A. N. Y., affirming S. C., 23 A. B. R. 304): "Of course, the trustee can after adjudication, and the receiver before, compel the surrender of assets in the possession of the bankrupt or of the alleged bankrupt or of any one for him. As to such persons the filing of the petition may be a caveat attachment and injunction. *Mueller v. Nugent* was just such a case."

However, the maxim quoted ordinarily is to be taken in the alternative; it operates in some cases as an attachment, in others as an injunction, etc. Thus it is not to be taken as literally accurate so far as it likens the operation of the filing in all instances to be the same, for example, in likening it to an "attachment," it certainly would not be so as to property not in the custody of the bankruptcy court. It would be misleading to say in all instances that the mere "filing" of the petition is "in effect an attachment." Such "filing" would operate as an attachment only where the property involved is in the custody of the bankruptcy court or is brought therein either through being in the possession of the bankrupt, or in that of a receiver or marshal of the court, but the mere "filing" certainly would not operate as an "attachment" under any doctrine if the bankruptcy court had no such custody; and no well considered case will be found so to hold.

Fidelity Trust Co. v. Gaskell, 28 A. B. R. 4, 95 Fed. 864 (C. C. A. Mo.): "It is true that the Supreme Court once said that the filing of a petition in bankruptcy is a caveat to all the world and in effect an attachment and an injunction * * * But the later decisions of that court adjudge that the statement quoted applies only to parties who have no substantial claim of a lien upon or title to the property claimed as that of the bankrupt and that against those who have such claims of existing titles or liens when the petition in bankruptcy is filed its filing is neither a caveat nor an attachment, that it creates no lien and that they are strangers to the proceedings in the absence of an order or process making them parties, or some equivalent notice."

Compare, *In re Mullen*, 4 A. B. R. 229, 101 Fed. 413 (D. C. Mass.): "If the rights of the trustee under § 70 (a), subd. 4, 5, and § 70 (e), are substantially those possessed by the creditors of the bankrupt under the law of Massachusetts, the trustee in this case cannot defeat the respondent's attachment unless the respondent shall be held, before the attachment, to have been affected with notice of the bankruptcy proceedings. I do not think that he was so affected. It has been said indeed, that bankruptcy proceedings affect with notice the whole world (*Bank v. Sherman*, 101 U. S. 403, 406, 25 L. Ed. 866); and this in spite of § 21 (e). See *Hall v. Whiston*, 5 Allen 126. But bankruptcy proceedings can hardly affect any one with notice that certain property standing in the name of a stranger belongs to the bankrupt."

Compare, *In re Mertens*, 15 A. B. R. 369, 144 Fed. 818 (C. C. A. N. Y.): "While the filing of a petition in bankruptcy is a caveat to all the world, the notice ought

not to have the effect of paralyzing all business dealings with the debtor, or to prevent lienors or pledgees from enforcing their contracts."

On the other hand the filing of the petition does operate, in a more or less qualified sense, as a "caveat" and "injunction" in that it affects all persons resorting to legal proceedings against the bankrupt or his property, and perhaps some others, with notice of the proceedings²⁸ and bids them beware. To that extent the property is in "custodia legis." Yet, further than this the maxim is not to be relied on as furnishing a working rule for actual practice and is rather high sounding than efficacious. The filing operates as an attachment sometimes and as an injunction sometimes, etc.

DIVISION 3.

TRUSTEE'S TITLE IN EXCESS OF BANKRUPT'S OWN TITLE AND IN EXCESS OF TITLE OF CREDITORS OUT OF BANKRUPTCY—HIS PECULIAR TITLE CONFERRED BY THE BANKRUPTCY ACT: VOIDABLE PREFERENCES AND INVALID LEGAL LIENS.

§ 1271. Third, Trustee's Peculiar Title and Rights Conferred by Bankruptcy Act Itself.—Third, then, as to cases where the title taken by the trustee is in excess of the bankrupt's own title, and also in excess of the title acquired by a levying creditor; where, in addition, it is the greater title conferred by the special provisions of the bankruptcy act itself.

In the orderly development of the treatise, the two subjects peculiar to bankruptcy law are now reached—the subjects of voidable preferences in bankruptcy and of the invalidity of liens obtained by legal proceedings, within the four months preceding bankruptcy; as well as the peculiar modification in the matter of proof of fraudulent transfers, permitted when the transfers occur within the four months preceding the bankruptcy.

§ 1272. Cases under This Subject Must Have Arisen Since Passage of Act.—Of course as to cases where the title is conferred by the special provisions of the bankruptcy act and is in excess of the bankrupt's own title, as well as of the title of creditors other than the trustee in bankruptcy, such cases can only be those that have arisen since the passage of the Bankruptcy Act.³⁰

§ 1273. General Discussion.—As previously noted,^{30a} bankruptcy law had its origin in the insufficiency of the ordinary remedies of English Common Law to protect creditors where there was a large number of creditors

²⁸ But compare, even on this point, *In re Zotti*, 26 A. B. R. 236, 186 Fed. 84 (C. C. A. N. Y.): "We think this language [*Mueller v. Nugent*, 184 U. S. 1, 7 A. B. R. 224] was never intended to be applied to a bank which has honestly paid checks of a depositor without notice that any petition in bankruptcy has been filed against him and who may never be adjudicated a bankrupt at all." By Bankr. Act,

§ 11; suits or dischargeable debts are ipso facto stayed see post, § 2695. Yet, it is to be observed that in the Southern District of New York the state courts in practice pay no attention to the pendency of bankruptcy proceedings unless a restraining order has been issued from the federal court.

³⁰ *Batchelder v. Whitmore*, 10 A. B. R. 641, 122 Fed. 355 (C. C. A. Mass.).

^{30a} See ante, "Introduction."

owed by a common debtor. The old remedies were well enough adapted to the protection of the creditor where there were only one or two creditors involved, but they fell short of doing justice where there was a large body of creditors interested in one insolvent estate.

The common law, as naturally might have been expected from the fact that it took its origin in a primitive and simple state of society where large commercial businesses built up on credit were impossible and the existence of a large body of creditors was unheard of, satisfied itself with the maxim "The law favors the diligent creditor." This maxim was high sounding and had the appearance of embodying the right principle, and perhaps it did express the complete rule proper for those days. By the term "diligent creditor," of course, was not meant the "diligent worker," the one who worked from early dawn to late at night, who worked conscientiously and gave full measure. It would perhaps seem right to give such one the first chance. But by the term "diligent creditor" was meant the creditor who was quickest to resort to legal action, who was least forbearing, least trustful and confiding in his debtor's honesty, as well as those who were the most alert. Before the present bankruptcy law was enacted, indeed, the "diligent creditor" in commercial law practice had come to mean most generally the creditor whom the debtor himself most favored, perhaps a friend or relative. It was this kind of a diligent creditor who was generally found first upon the field. And so, the maxim that "the law favors the diligent creditor," came to be inadequate to the doing of justice in cases of insolvency in this period of large commercial dealings on credit. The maxim quite lost its dignity in these modern commercial times. Indeed, precisely through this want arose bankruptcy law, which is founded upon entirely different principles, upon the broad and noble maxims of equity that "Equality is equity," and "He that asks equity must do equity." In bankruptcy law the creditor who first resorts to legal proceedings to seize his debtor's property gets no advantage over his fellow creditors; nor does the creditor whom the debtor favors by paying him in full out of the insolvent estate to the loss of others. The maxim "Equality is equity" governs—not the maxim "the law favors the diligent creditor." The unseemly scramble to be first on the scene, that was the general incident to business failures a few years ago, no longer takes place. The wild race between the sheriff, with his attachments and executions, and the receiver, to get ahead of the inevitable preferred mortgagee and friendly assignee for the benefit of creditors is a thing of the past; under the regime of the Bankruptcy Act "equality is equity." No longer is it that "the law favors the diligent creditor."

In re American Brewing Co., 7 A. B. R. 468, 112 Fed. 752 (C. C. A. Ills.): "The avowed purpose of taking the judgment notes, with power to enter judgment at any time by confession, was to secure appellants against the claims of other creditors, and to give them a preference. That would be legitimate

and proper if no Bankrupt Law were in force, and a race of diligence in priority were allowable. But one purpose and effect of the Bankrupt Law is to put an end to such a race of diligence, and to divide the estate ratably among creditors. The essential ethics of that law is that 'equality is equity.'

To use an illustration, it is as if a meagre table were set for a hungry crowd. Common law says to each one "Seize all you can, and as quickly as you can, no matter if the rest get nothing: 'first come, first served' is the rule." Bankruptcy law, on the other hand, says "No, let a fairer rule prevail: let considerateness govern. Let each one take his proportionate share. The meal is too scanty, to be sure, to satisfy all. No one can satisfy fully his wants; but, on the other hand, no one shall be crowded out, no matter how weak or poor he may be or how slow he may have been in getting to the table: each shall have his share." And so have been developed the two striking and distinguishing features of bankruptcy law—that creditors receiving (under certain qualifications and limitations) more than their proportionate share out of the debtor's insolvent estate must surrender the preference into the common fund for all; and that the seizure of property of the insolvent estate (under other certain limitations) by legal proceedings are also void and this property also must be surrendered to form part again of the common fund for all.

Compare, *In re Hopkins*, 1 A. B. R. 209 (Ref. Ala.): "The Bankruptcy Act of 1898 recognizes and affects two different classes of liens, 1st, those created by the acts of the parties (preferences): second, those acquired by creditors under and by virtue of legal proceedings."

Compare, *Farmers' Bank v. Carr*, 11 A. B. R. 733, 127 Fed. 690 (C. C. A.): "The essential principle of the bankrupt law is that all of the bankrupt's property be divided equally, without preference, to the payment of his debts. It abhors preferences."

§ 1274. "**Trust Fund,**" **Theoretical Basis of Peculiar Titles Conferred by Bankruptcy Act.**—Now, what theory lies at the basis of these peculiar provisions of bankruptcy law? Why may not an insolvent debtor pay in full whatsoever creditor he prefers to pay, notwithstanding the remainder may get nothing at all or only a small per cent of their respective claims, so long as the debt paid is an honest and just debt? Why, also, may not a creditor seize and hold by legal process property of the insolvent debtor in satisfaction of his just and due claims? Why is it not permitted to the first creditor who levies to get all he can up to the amount of his full claim; then to the creditor who chances to be second and not first in levying, to get all the rest up to the amount of *his* claim; and so on with the third and fourth till all the property is exhausted? and why is it not right that those who do not act quickly enough, who happen to be fourth or fifth or tenth or twentieth in levying, get nothing at all to apply upon their claims? Common law has declared that all this really is right; and it says it is so because manifestly it is right that whatever the debtor owns he has on his part a perfect right to use in paying his debts and the creditor on

his part to take in payment of his claim. But in the light of bankruptcy law the answer to these questions is different. The answer is simply this: In law the insolvent debtor does own the property belonging to his insolvent estate; but in equity, as developed in the bankruptcy law—at least, if we view the matter from the standpoint of the philosophy of the law—he does not absolutely own it. The insolvent estate is, in theory, a trust fund. While the courts have refused to announce such doctrine as an established principle of general law outside of bankruptcy jurisprudence, and have not enunciated it, in so many words even in bankruptcy jurisprudence, yet some such theory must be the principle of justice on which the peculiar rights conferred by the act really rest. It is only upon some such theory as this of the trust fund that the requirement of surrender of preferences and the return of property seized on legal process can be justified in cases of insolvent estates. Only so can the debtor's right to use what at common law is his own property in the payment of any just debt he may prefer to pay be restricted, and the creditor's right to seize his debtor's property in satisfaction of his just claim be thwarted.

The insolvent estate is, in the philosophy of the law, if not in the announced decisions, not his own—that is the answer.

He *is not* using his *own* property with which to pay his debts. He has used up all his own property, as equity looks at it, and this is precisely why he has become insolvent; he is now making use of the common fund contributed by all his creditors. As long as he remains solvent, he may do with his property as he sees fit, for it is his own both in law and also in equity; but the moment he becomes insolvent he ceases to be using up his own capital; and so at the moment of insolvency, equity, in the form of bankruptcy law, steps in and declares his property a trust fund belonging to all his creditors.

In *re McGee*, 5 A. B. R. 262, 105 Fed. 895 (D. C. N. Y.): "In either instance the property which theoretically at least belongs to all creditors is taken from them and given to a favored creditor—a situation which the Bankruptcy Act was passed to prevent."

This seems to be the theory underlying the treatment in bankruptcy of preferences and legal liens obtained within four months preceding bankruptcy.³¹

In *re Keller*, 6 A. B. R. 340, 109 Fed. 118 (D. C. Iowa): "The Bankrupt Act may be said to be based upon two fundamental propositions: First, that when a person becomes unable to pay his just debts, the property then remaining to him equitably belongs to his creditors, and should be distributed proportionately among them; and, second, that, if the insolvent debtor in good faith yields up to his creditors his property for distribution among them, he should then be relieved from the debts existing against him at the time he transfers his property to his creditors. The first proposition is not based upon the ques-

31. *White v. Bradley Timber Co.*, 9 A. B. R. 442 (D. C. Ala.).

tion of good faith on the part of the debtor, nor upon his knowledge or want of knowledge of his actual financial condition. It rests upon the fact of insolvency; and the equity in favor of the creditors grows out of the fact that it is ordinarily true that the estate possessed by the insolvent debtor represents the goods, property or money obtained by the debtor on credit from his creditors. If in fact the debtor is insolvent, and if in fact he has in possession property which he has bought on credit and which has not been paid for, is not the equity in favor of the creditors fully established, without reference to the mere belief which the debtor may entertain with respect to his ability to pay his debts? It is a matter of common knowledge that persons who are hopelessly insolvent will frequently cling to the belief that they can pay up if only allowed a little time, yet, if time be allowed them, they only become more heavily involved. It cannot, therefore, be successfully maintained that the equity of creditors to the estate of an insolvent debtor is in any true sense dependent upon or affected by his belief touching his actual condition. This equity cannot, however, be carried into effect except through legal machinery; and to that end, among others, the present Bankrupt Act has been adopted. When, through the provisions of that act, an estate of an insolvent debtor has been brought before the court of bankruptcy for distribution, is it not true that among the creditors the general rule is that 'equality is equity;' that is to say, that in the division of the estate each creditor shall receive only his proportionate share of the estate? It must be remembered that the institution of the proceedings in bankruptcy does not create the equity in favor of the creditors, but only sets in motion the machinery by which the equity can be properly enforced. The equity on behalf of the creditors comes into existence when the debtor becomes insolvent."

Swarts v. Fourth Nat'l Bk., 8 A. B. R. 677, 117 Fed. 1 (C. C. A. Mo.): "The dominant purpose of the prohibition of a preference was not to benefit or injure, or to prevent the benefit or injury, of any creditor or class of creditors, but to prevent the debtor from making any disposition of his property which would prevent its equal distribution—to prevent him from doing anything which would result in the payment out of his property of a larger percentage upon any claim than others of the same class would receive."

In re Schafer, 5 A. B. R. 149, 3 N. B. N. & R. 145 (Ref. N. Y.): "This view is supported by what I conceive to have been the intent of the Congress in the enactment of the bankruptcy law. The underlying idea appears to be that at the moment when a person becomes insolvent, that is, within the definition of the term at § 1, subdivision 15—'Whenever the aggregate of his property * * * shall not at a fair valuation be sufficient in amount to pay his debts'—the property then remaining with the insolvent belongs to his creditors, and to all creditors of the same class pro rata, in equal proportion to their contributions thereto. No preferences among creditors in the same class are intended to be tolerated by the bankrupt law. The purpose of the act was to accomplish such equal distribution as nearly as practicable."

Compare, (1867) *In re Reiman & Friedlander*, 11 Nat. Bankr. Reg. 34: "The principle upon which the law of bankruptcy has, in legislation, been founded, is that when a man becomes insolvent, the property then remaining to him rightfully belongs to his creditors, and ought to be distributed ratably among them towards the satisfaction of their claims."

§ 1275. Efficiency of Facts to Create Passing of Title and Nature of Title Passing, Determined by State Law.—It must be reiterated

that although the Bankruptcy Act itself creates new rights, those to preferentially transferred property and property seized by legal proceedings within the four months preceding the bankruptcy—yet the law of each state determines the sufficiency of the transaction to constitute a “pledge” or “mortgage,” a “sale,” a “legal lien,” or other appropriation of property. The law of the State, it must not be forgotten, all the time, determines the nature or name, so to speak, of the transaction and the time of the passing of title thereby, [except as the Amendment of 1910 to § 60 (b) changes the date of such passing of title] whereupon the Bankruptcy Act steps in and declares that, having such name and title thus passing, it is or is not a voidable transaction.

All this has been previously covered—see ante, § 1139, et seq.—but its pertinency is so great in connection with a discussion of the law of preferences that it bears repetition.^{31a}

At the risk of some repetition, we have thus taken a preliminary survey of the general nature of these two peculiar and important provisions of bankruptcy law, and thus by understanding the theory and principles underlying them are in a better position to take up their formal study in detail. And first, as to preferences:

SUBDIVISION “A.”

VOIDABLE PREFERENCES.

§ 1276. Definition of Preference.—Section 60 (a) as originally enacted defined a preference as follows:

“A person shall be deemed to have given a preference, if, being insolvent, he has procured or suffered a judgment to be entered against himself in favor of any person, or made a transfer of any of his property, and the effect of the enforcement of such judgment or transfer will be to enable any one of his creditors to obtain a greater percentage of his debt than any other of such creditor of the same class.”

Swarts v. Fourth Nat. Bk., 8 A. B. R. 673, 117 Fed. 1 (C. C. A. Mo.): “Section 60 (a) furnishes the legal and controlling definition of the preference specified in § 57 (g) and other parts of the Bankrupt Act.”

By the amendment of February, 1903, the further limitation was added that, in order to constitute such judgment or transfer a preference it must have been taken or made within four months preceding the bankruptcy; so that the section defining the term preference as used in bankruptcy now reads as follows:

“A person shall be deemed to have given a preference if, being insolvent, he has, within four months before the filing of the petition or after the filing of

31a. Compare, also, in re *Ball*, 10 A. B. R. 565, 123 Fed. 164 (D. C. Vt.): “The title to the other goods as well as these is governed by the laws of the

State, although what is a preference under the Bankrupt Law must be controlled by that.”

the petition and before the adjudication, procured or suffered a judgment to be entered against himself in favor of any person, or made a transfer of any of his property, and the effect of the enforcement of such judgment or transfer will be to enable any of his creditors to obtain a greater percentage of his debt than any other of such creditors of the same class. Where the preference consists in a transfer, such period of four months shall not expire until four months after the date of the recording or registering of the transfer if by law such recording or registering is required."

Section 60 (b) as amended in 1910 defines the circumstances under which the preference is voidable for the benefit of all creditors as follows:

"If a bankrupt shall have procured or suffered a judgment to be entered against him in favor of any person or have made a transfer of any of his property, and if, at the time of the transfer, or of the entry of the judgment, or of the recording or registering of the transfer if by law recording or registering thereof is required, and being within four months before the filing of the petition in bankruptcy or after the filing thereof and before the adjudication, the bankrupt be insolvent and the judgment or transfer then operate as a preference, and the person receiving it or to be benefited thereby, or his agent acting therein, shall then have reasonable cause to believe that the enforcement of such judgment or transfer would effect a preference, it shall be voidable by the trustee and he may recover the property or its value from such person."

§ 1277. "Preferences," "Voidable Preferences" and "Preferences" That Are "Acts of Bankruptcy," to Be Distinguished.—It must be noted that a preference itself is one thing and a preference that amounts to an act of bankruptcy sufficient to throw a debtor into bankruptcy is the same thing and more; and that a preference which can be avoided by the trustee, so that the property affected by it can be recovered for the benefit of all the creditors, is the same thing and also something more, but that that "something more" is still different.

Thus, a preference in fact may exist even if the debtor did not intend or know that his transfer would result in a preference, and so be insufficient grounds for throwing him into bankruptcy; and it may also exist even if the creditor took it without any cause appearing to him for believing that a preference would be effected thereby, and so may not be sufficient grounds for the creditors to retake possession of the property transferred; for the question as to whether the transfer is or is not a preference is to be determined solely by results, independently of the debtor's intent and independently of the creditor's participation therein; and the questions of intent, etc., with which the preference was given or received simply touch the effect on the debtor's and creditors' respective rights.³²

³² In re Bashline, 6 A. B. R. 194 (D. C. Pa.); In re Keller, 6 A. B. R. 334, 109 Fed. 118 (D. C. Iowa); In re Conhaim, 3 A. B. R. 251, 97 Fed. 295 (D. C. Dist. Wash.); In re Fixen & Co., 4 A. B. R. 10 (C. A. Calif.); In re Carson, Pirie, Scott & Co., 5 A. B. R. 814 (U. S. Sup. Ct.);

Benedict v. Deshel, 11 A. B. R. 22, 177 N. Y. 1: "In unmistakable language Congress has said that when an insolvent debtor makes a transfer of property, the effect of which will be to enable any one of his creditors to obtain a greater percentage of his debt than any other creditor of the same class **'the debtor shall be deemed to have given a preference.'** Shall this language be held to be meaningless? Shall it be expunged from the statute by judicial construction? * * * The statute deals with three distinct legal en-

compare *Western Tie & Timber Co. v. Brown*, 12 A. B. R. 111, 129 Fed. 728 (C. C. A. Ark.).

Elements of a Preference as Laid Down in Decisions—Before Amendment of 1910.—In *re Sayed*, 26 A. B. R. 444, 185 Fed. 962 (D. C. Mich.); *Morris v. Tannenbaum*, 26 A. B. R. 368 (Ref. N. Y.); *Sebring v. Wellington*, 6 A. B. R. 672 (N. Y. Sup. Ct. App. Div.): Where the court enumerates the elements of a preference that are recoverable from the creditor as being four. *Hastings v. Fithian*, 13 A. B. R. 678 (Ct. Errors & Appeals N. J.); *Painter v. Napoleon Township*, 19 A. B. R. 412, 156 Fed. 289 (D. C. Ohio), quoted at § 1385.

Baden v. Bertenshaw, 11 A. B. R. 309, 68 Kans. 32: "If a payment intended as a preference is made within four months before the filing of a petition in bankruptcy, and the creditor believed, or had reasonable cause to believe, that it is intended to give a preference, and such payment has the effect to enable such creditor to obtain a greater percentage of his debt than other like creditors, the trustee may recover the amount so paid, regardless of any fraudulent intent." In *re Armstrong*, 16 A. B. R. 592 (D. C. Iowa).

McDonald v. Clearwater R. Co., 21 A. B. R. 182, 164 Fed. 1007 (U. S. C. C. Idaho): "Upon his own theory, therefore, before plaintiff can succeed in avoiding the alleged preference, the existence of four conditions must be made to appear: First, that the lumber company was insolvent when the assignment was made; second, that the assignment was made upon account of an antecedent indebtedness; third, that the bank had reasonable cause to believe that, by the assignment, it was intended ["intended" changed by Amendment of 1910 to "would be effected"] to give a preference; and, fourth, that the effect of the assignment was to enable the bank to obtain a greater percentage of its debt than other creditors of the same class."

Wright v. Skinner Mfg. Co., 20 A. B. R. 527, 162 Fed. 315 (C. C. A. N. Y.): "It is necessary for the trustee in order to recover under § 60, to es-

tablish the following propositions: First: That the payments were made within four months before the filing of the petition. Second: That at the time of the payments the bankrupt was insolvent within the meaning of subd. 15, § 1, of the act. Third: That the effect of the payments was to give the defendants a greater percentage of their debts than other creditors of the same class. Fourth: That the defendants had reasonable cause to believe that it was intended ["intended" changed to "would be effected" by Amendment of 1910] by such payments to give them a preference."

Tumlin v. Bryan, 21 A. B. R. 319, 165 Fed. 166 (C. C. A. Ga.): "The burden of proof is on the complainant, and, unless he shows by sufficient evidence the elements of a voidable preference, he is not entitled to recover. He must prove that the bankrupts (1) while insolvent, (2) within four months of the bankruptcy, (3) made a transfer of their property, i. e., a payment of money, (4) and that the creditor receiving the payment was thereby enabled to obtain a greater percentage of his debt than other creditors of the same class; and it must also be proved (5) that the person receiving the payment, or to be benefited thereby, had reasonable cause to believe that it was thereby intended to give a preference. Bankruptcy Act, § 60, cls. 'a' and 'b.'"

In *re Leech*, 22 A. B. R. 599, 171 Fed. 622 (C. C. A. Ky.): "In order to establish that there was an unlawful preference, it must be alleged and proven that at the time of the transfer the party making it was insolvent, that the property transferred was such as his creditors had a right to have subjected to their claims, that he intended a preference, and that the transferee had reasonable cause to believe that the transferer had such an intention."

Taylor v. Nichols, 23 A. B. R. 310, 134 App. Div. 787: "Two facts were required to be proven in order to justify the judgment rendered: First, that at the time of the transfer William H. Nichols was insolvent; and, second, that this defendant had reason

tities concerned in the administration of a bankrupt's estate: 1. The debtor. 2. The trustee. 3. The creditor. As to the debtor, the statute declares that a payment under certain conditions shall be held to be preferential. He is not to be heard upon the question of his intent. The effect of his act is fixed by law. That is the scope and purport of subdivision a. The next section, subdivision b, declares, in effect, that a preferential payment is not void per se, but voidable by the trustee upon a certain condition. And what is the condition? Simply that the trustee shall establish that the creditor had reasonable cause to believe that the payment to him was intended as a preference. [Changed by the Amendment of 1910, to "would effect a preference."] In other words, the trustee's remedy is not absolute, but is made to depend upon proof of the knowledge or belief with which the creditor took the payment. * * * In each case the condition affixed to the remedy ignores the state of mind of one of the parties to the transaction and renders his act dependent upon the purpose of the other."

Swarts v. Fourth Nat'l Bk., 8 A. B. R. 677, 117 Fed. 1 (C. C. A. Mo.): "The meaning and effect of § 60 (a) are the same as though it declared every transfer of his property by an insolvent to be a preference which has the effect to 'enable any one of his creditors to obtain a greater percentage of his debt' out of the property of the insolvent 'than any other of such creditors of the same class.'"

to believe that the transfer was made with intent to give him a preference."

Since Amendment of 1910.—*Mayes v. Palmer*, 31 A. B. R. 225, 208 Fed. 97 (C. C. A. Mo.): "To entitle the trustee to a decree it was necessary that it appear: First, that William W. Reid was insolvent at the time of the transfer; second, that the transfer was made within four months of the filing of the petition in bankruptcy; third, that the effect of the transfer would be to enable Charles A. Mayes to obtain a greater percentage of his debt than other creditors of the same class; and fourth, that Charles A. Mayes had reasonable cause to believe that it was intended by the transfer to give such preference." [This court ignores the fact that the Amendment of 1910 changed the law from "intended" to "would effect."]

Newman v. Dry Goods Co., 31 A. B. R. 399 (Kansas City Court of Appeals): "Four elemental facts must combine to render a preference voidable viz: First, the insolvency of the debtor, at the time of the preference, and by insolvency, as that and equivalent words are defined in the existing law, reference is made not to a person who 'was unable to pay his debts as they became due in the ordinary course of his daily transactions,' but one whose property 'shall not, at a fair valuation, be sufficient in amount to pay his debts.' In re Louis A. Eggert (D. C. Wis.), 3 Am. P. R. 541, 98 Fed. 843. Second, the

giving of the preference within four months of the petition in bankruptcy. Third, the effect of securing to the favored creditor a greater percentage of his debt than other creditors of the same class may obtain from the estate of the debtor. Fourth, that the preferred creditor, when he received the preference, knew or had reasonable cause to believe that it was the purpose of his debtor to give him a preference over other creditors of the same class. See *Gill v. Safe Co.*, 170 Mo. App. loc. cit. 485, 156 S. W. 811." [This court ignores the fact that the Amendment of 1910 changed the law from "intended" to "would be effected."]

In re *Starkweather & Albert*, 30 A. B. R. 743, 206 Fed. 797 (D. C. Mo.): "To constitute a voidable preference under this provision of statute, the following must concur: 'The bankrupt must (1) have made a transfer of its property (2) within four months of the filing of the petition in bankruptcy, and (3) at the time of the transfer the bankrupt must have been insolvent. (4) The transfer must have operated as a preference; i. e. (§ 60a), its effect must have been to enable the bank to obtain a greater percentage of its debt than other creditors of the same class received. Further, the bank or its agent was (5) at the time of the transfer have had reasonable cause to believe that the enforcement of such transfer would effect a preference.'"

Of course the classification here adopted is simply for the purpose of the author's analysis of the subject and does not pretend to be founded on any classification formally made by any court.

A preference itself has eight elements, which are as follows:

§ 1278. First Element of a Preference—Depletion of Insolvent Fund.—Some portion of the debtor's property must have been appropriated by the transaction and the insolvent estate thereby diminished. Preference implies appropriation of assets and depletion of the trust fund thereby.³³

Bank of Newport v. Herkimer Co. Bank, 225 U. S. 178, 28 A. B. R. 218, affirming *Mason v. Herkimer Co. Bank*, 22 A. B. R. 733, 172 Fed. 529 (C. C. A. N. Y.): "But, unless the creditor takes by virtue of a disposition by the insolvent debtor of his property for the creditor's benefit, so that the estate of the debtor is thereby diminished, the creditor cannot be charged with receiving a preference by transfer."

Trust & Savings Bank v. Trust Co., 229 U. S. 435, 30 A. B. R. 624: "To constitute a preferential transfer within the meaning of the Bankruptcy Act there must be a parting with the bankrupt's property for the benefit of the creditor, and a consequent diminution of the bankrupt's estate."

§ 1279. Entirely Fictitious Transactions.—Thus, an entirely fictitious transaction, where no property is actually taken, cannot constitute a preference.

In *re Steam Vehicle Co. of Am.*, 10 A. B. R. 385, 121 Fed. 939 (D. C. Pa.): "Neither, under the provisions of the Bankrupt Act, can the claimant be properly held to have received a preference. It never received a cent of money or any other consideration on account of the disputed items. No gain has come to it, and no loss has come to the bankrupt, because of what was done; and therefore, as it seems to me, it is impossible to hold that mere juggling with book entries amounts to payment. As I look at the matter, payment means at least that value has passed in some form or other; and the word does not properly embrace a fictitious transaction, such as this, where no value was intended to pass, and where none was actually transferred. Reprehensible as the conduct under consideration was, and whatever its effect might be in other proceedings, it did not do the slightest harm to the other creditors, and did not take from them any part of the bankrupt's assets."

So, also, a void transfer cannot amount to a preference.³⁴

A like result would be obtained, even though the parties actually believed that a transfer had been effected, if, in fact, nothing passed; as, for instance, where one goes through the form of transferring his rights under a revocable privilege which had been revoked prior to the attempted transfer thereof.³⁵

^{33.} *Aiello v. Crampton*, 29 A. B. R. 1, 201 Fed. 891 (C. C. A. N. Mex.).

^{35.} In *re Martin*, 29 A. B. R. 623, 200 Fed. 940 (C. C. A. N. J.).

^{34.} *Rosenbluth v. DeForest, etc., Co.*, 27 A. B. R. 359 (Sup. Ct. Conn.).

§ 1279¼. **Transferring Worthless Equity.**—The transfer of an equity of redemption where the lien exceeds the value of the property is not a preference—the estate is not depleted.³⁶

§ 1279½. **Trivial Transfers.**—The court sometimes will disregard a transaction alleged to be a preferential transfer, because of its triviality, thus, the payment by a grocery firm, of a bill of \$3.00 to a creditor a week before the bankruptcy;³⁷ again, the transfer of a worthless account.

In re Hamilton Automobile Co., 31 A. B. R. 205, 209 Fed. 596 (C. C. A. Ills.): "The Bankruptcy Act deals with matter of substance and the mere preferential transfer of a worthless claim does not come within the meaning of the Act."

Likewise, the payment by an old bachelor, of 60 cents for soda water, coca cola and a bar of soap, and \$2.15 for a "dressed doll" have been disregarded as preferential.³⁹

§ 1280. **Performance of Labor in Payment of Debt.**—Likewise, the performance of labor in payment of a debt has been held not a transfer of property, hence, not a preference.⁴⁰

In re Abraham Steers Lumber Co. (Steers Lumber Co.), 6 A. B. R. 315, 110 Fed. 738 (D. C. N. Y., affirmed 7 A. B. R. 332, 112 Fed. 406): "The labor, credited August 28, and amounting to \$37.17, may be offset, as it cannot be regarded as a transfer of property."

§ 1280½. **Taking Possession of One's Own Property.**—Of course where one takes his own property out of the possession of the bankrupt, even though within the four months period and whilst the bankrupt was insolvent, it is not a preference.⁴¹

In re Wright—Dana Hardware Co., 30 A. B. R. 582, 207 Fed. 636 (D. C. N. Y.): "On the day of the adjudication in bankruptcy the Warren Paint Company repossessed itself of all the paint then in the warehouse of the bankrupt as its own, and the trustee claims that by so doing it received a preference, and cannot prove and have its claim allowed until it has surrendered such preference. It is self-evident that if the paint taken by the Warren Paint Company was its own property, absolute, it had the right to take possession, and that the taking created no preference."

36. (1867) Catlin v. Hoffman, 9 Nat. Bank Reg. 342.

37. Obiter, In re Stovall Grocery Co., 20 A. B. R. 537, 161 Fed. 882 (D. C. Ga.).

39. Macon Grocery Co. v. Beach, 19 A. B. R. 558, 156 Fed. 1009 (D. C. Ga.).

40. See post, § 1333. Compare, analogously (as to not refusing discharge), In re Fitchard, 4 A. B. R. 609, 103 Fed. 742 (D. C. N. Y.). Compare, analogously (as to not refusing discharge), In re Adams, 4 A. B. R. 696 (D. C. N.

Y.). Compare, analogously, In re Howe Security Co., 17 A. B. R. 181 (D. C. Ala.); In re Adams, 22 A. B. R. 613, 171 Fed. 599 (D. C. N. Y.); In re Thaw, 24 A. B. R. 759, 180 Fed. 419 (D. C. Pa.), quoted at § 2747.

"Good will," transfer of, when a preference, compare, McElvain v. Hardesty, 22 A. B. R. 320, 169 Fed. 31 (C. C. A. Mo.).

41. Instance, purchaser of cotton, who is paid in advance on pledged bills of lading, attaching the cotton on arrival, Boden & Haac v. Lovell, 30 A. B. R. 353, 203 Fed. 234 (C. C. A. Ala.).

§ 1281. **Liens Given within Four Months in Fulfillment of Promise Made before.**—A chattel mortgage or other lien given within the four months, in fulfillment of a promise to execute one made before the four months period, constitutes a preference, for the mere promise to give the mortgage did not operate to appropriate the property, and so the appropriation took place within the requisite statutory period;⁴² so, as to other transfers made in pursuance of prior agreements.⁴³

§ 1282. **No Preference by "Judgment" unless Judgment Operates to Create Lien or Otherwise to Appropriate Property.**—A judgment even if "suffered or procured" by the bankrupt to be taken, nevertheless will not amount to a preference unless thereby some property is so sequestered, or a lien obtained upon it, that the enforcement of the judgment would deplete the estate, for the word "judgment" as used in this § 60 (a) means an effective judgment—a judgment whereby property of the bankrupt is in some way appropriated. Therefore, a merely personal judgment, where no lien results, would, of course, not amount to a preference, until levy of execution thereunder.⁴⁴ It would not deplete the trust fund belonging to all the creditors, which is the touchstone of a preference.

Again, an attachment on mesne process before the four months' period not yet followed by judgment before the filing of the bankruptcy petition has been held not to constitute a preference.⁴⁵

§ 1283. **Giving of Check or Note Not Preference; but Paying of It Is.**—The giving of the debtor's check or note or other instrument of in-

42. See post, this subdivision, "Sixth Element of a Preference; Four Months Limit," § 1376.

Taking of possession under unrecorded mortgage—whether appropriation takes effect as of date of taking possession or date of execution of mortgage: Effect of mortgage to cover future-acquired property, acquired during the four months period: See *Humphrey v. Tatman*, 14 A. B. R. 74, 198 U. S. 91 (reversing *Tatman v. Humphreys*, 12 A. B. R. 62, 184 Mass. 361).

These subjects are involved in previous discussions (ante, §§ 1139, 1140, 1209) as to the Local Law governing in determining the Trustee's title as the successor of creditors, as also in determining his title as conferred by the peculiar provisions of the Bankruptcy Act.

A chattel mortgage executed in blank, before the four months period, but not filled in with the amount of the debt until within the four months period, takes effect only from the date of the filling in, and is a preference. In *re Barrett*, 6 A. B. R. 48 (D. C. N. Y.).

43. *Roy v. Salisbury*, 27 A. B. R. 892 (Sup. Ct. N. Y.).

44. Bankr. Act, § 60 (a); In *re Pease*, 4 A. B. R. 547 (Ref. N. Y.); instance, In *re Metzger Toy & Novelty Co.*, 8 A. B. R. 307 (D. C. Ark.); inferentially, *Wilson Bros. v. Nelson*, 7 A. B. R. 142, 183 U. S. 191.

45. In *re Crafts-Riordan Shoe Co.*, 26 A. B. R. 449, 185 Fed. 931 (D. C. Mass.): "That an attachment on mesne process under Massachusetts law not yet followed by judgment, is not enough in itself to constitute a preference obtained by the plaintiff would seem to follow from *Parmenter Co. v. Stover*, 3 A. B. R. 220, 97 Fed. 330 (C. C. A. Mass.) * * * in the cases which have held preferences to have been obtained through legal proceedings and an attachment has formed part of the proceedings, attachment has been either after one judgment in suit, or, if before judgment, has been followed by a judgment before the petition in bankruptcy, so that the attachment will have passed beyond the stage during which it is uncertain whether there is really any claim against the defendant or not."

See also, § 1455.

debtedness is not the giving of the preference;⁴⁶ but it is the payment of it out of the bankrupt's estate that is the preference;⁴⁷ and even where a purchaser of the bankrupt's stock gave his note to the creditor as part of the price it has been held not to be a preference until paid.

Compare, instance, *Opp v. Hakes*, 15 A. B. R. 700, 142 Fed. 364 (C. C. A. Ills.): "The appellant has not been paid the amount of the note which constitutes the alleged preference, and, without proof of other circumstances to charge him with such amount, the equitable remedy is surrender of the note, if preferential, and not its assumed value." This decision seems to be wrong on principle, the giving of the note was part of the consideration paid for the transfer and, presumably, pro tanto, diminished the money payment.

§ 1284. Payment Actually Made Not to Be Applied to Evade Preference Statute.—A payment actually made afterwards, cannot be applied on an unpaid note or check made before a certain invoice was sold on credit to the bankrupt, so as to entitle the creditor to offset the invoice against the payment as being a "subsequent credit."⁴⁸

§ 1285. Payment by Bankrupt of Own Note Discounted by Creditor, a Preference.—But where the creditor discounts the bankrupt's note at a bank its payment within the four months by the bankrupt constitutes a preference to the creditor, the bankrupt's estate being depleted thereby.⁴⁹

§ 1285½. Payment to Holder, Preference to Accommodation Endorser.—It has also been held that a payment to a holder may be a preference to an accommodation endorser.⁵⁰

46. *National Bank of Newport v. Herkimer Co. Bank*, 28 A. B. R. 218, 225 U. S. 178, quoted at § 1278.

47. In *re Harrison Bros.*, 28 A. B. R. 684, 197 Fed. 320 (D. C. Pa.); In *re Lyon*, 10 A. B. R. 25, 121 Fed. 723 (C. C. A. N. Y., affirming although on this point correcting, 7 A. B. R. 412). In this instance the check was post-dated and the insolvency was proved only as of the date of the payment. In *re Wolf & Levy*, 10 A. B. R. 153, 122 Fed. 127 (D. C. Tenn.); In *re Bailey*, 7 A. B. R. 26 (D. C. Vt.); obiter, *Upson v. Mt. Morris Bk.*, 14 A. B. R. 6 (N. Y. Sup. Ct. App. Div.).

Reviving Outlawed Debt on Eve of Bankruptcy to Enable Creditor to Participate in Dividends.—The revival by the bankrupt of an outlawed debt on the eve of bankruptcy, though made with the intent of enabling a creditor to participate in the dividends has been held not to be a fraud on creditors or a preference the creditor having no reasonable cause to believe the payment would operate as a preference. In *re*

Banks, 31 A. B. R. 270, 207 Fed. 662 (D. C. N. Y.).

48. In *re Bailey*, 7 A. B. R. 26 (D. C. Vt.): Although this was a case of so-called "innocent" preference not cognizable since the amendment of 1903, yet the principle decided is not affected by the amendment. Compare analogous principle involved in *Hackney v. Hargreaves Co.* (Raymond Bros. Clark Co.), 13 A. B. R. 164, 68 Neb. 676. Also compare analogous principle where creditor applied payments on nonpriority part of his claim to leave priority part unpaid. In *re King*, 7 A. B. R. 619 (D. C. Mass.).

49. In *re Matthews & Rosenkrans*, 15 A. B. R. 721 (Ref. Mass.).

A fortiori (payment to holder held preference to accommodation endorser), obiter (reasonable cause for belief not shown). *Reber v. Shulman & Bro.*, 24 A. B. R. 782, 179 Fed. 574 (D. C. Pa.).

50. Obiter (reasonable cause to believe not proved), *Reber v. Shulman & Bro.*, 24 A. B. R. 782, 179 Fed. 574 (D. C. Pa.).

§ 1286. Return of Loan Made for Specific Purpose, Not Preference.—The return of a loan made for a specific purpose, upon the purpose failing, is not a preference.⁵¹ But by this is not meant that the repayment of a loan made for a specific purpose, where the borrower has used it for another purpose, is not preferential; the identical property or fund must be that which is returned, else a preference may exist.

In *re Kearney*, 21 A. B. R. 721, 167 Fed. 995 (D. C. Pa.): "Upon the foregoing facts, it is clear, I think, that the payment on May 25th to the bankrupt's brother was preferential. Even if it was intended at the time when the loan was made that the money should be used for the specific purpose of paying for the license, and, if not so used, that it should be returned, the testimony seems to show plainly that this intention was not carried out, but that the bankrupt used the money for some other purpose. No effort was made on his behalf to prove what he had done with it. * * * Since, therefore, the money was not traced into a particular fund or deposit, or earmarked in any other way, the inevitable inference is that the check of May 25 was drawn against the general funds of the bankrupt, and was intended to prefer."

§ 1286½. Return of Bailed Property, Not Preference.—The return of bailed property to the bailor of course is not a preference—the bailee's estate has not been depleted.⁵²

§ 1287. Discounting of Bankrupt's Note, Not Preference.—And the discounting of the bankrupt's note by a third party does not constitute a preference, even though the discount money is applied upon the bankrupt's debt; the depletion of the bankrupt estate, and consequently the preference, not occurring until the bankrupt pays the note.⁵³

§ 1288. Payments by Sureties and Endorsers of Bankrupt, Not Preferences.—Payments by sureties and endorsers of the bankrupt, of course, do not constitute preferences and need not be surrendered by the creditor.⁵⁴

Mason v. Herkimer Co. Bank, 22 A. B. R. 733, 172 Fed. 529 (C. C. A. N. Y.): "The one thing absolutely essential to a preference is that the bankrupt transfer some portion of his property to the creditor. If the creditor

⁵¹ *Dressel v. North State Lumber Co.*, 9 A. B. R. 541, 107 Fed. 225 (D. C. N. Car.).

⁵² Compare, cases cited under § 1228; also, see *Walther v. Williams Mercantile Co.*, 22 A. B. R. 328, 169 Fed. 270 (C. C. A. Mich.), wherein the bailment of an entire business was upheld and the bailor's repossessing himself of it held not to be a preference, the bailment being on the terms that the bailees should keep the stock replenished and pay the bailor's commissions on gross sales, the bailors on their part to pay any excess of value over original value on repossession.

⁵³ *National Bank of Newport v. National Herkimer Co. Bank*, 28 A. B. R. 218, 225, U. S. 178, quoted at § 1300. Inferentially, see *In re Lyon*, 10 A. B. R. 25, 121 Fed. 123 (C. C. A. N. Y.); compare *In re Meyer*, 8 A. B. R. 598 (D. C. Tex.); compare *In re Waterbury Furn. Co.*, 8 A. B. R. 79, 114 Fed. 225 (D. C. Conn.); contra, *In re Weissner*, 8 A. B. R. 177 (D. C. N. Y.).

⁵⁴ *Swarts v. Fourth Nat'l Bk.*, 8 A. B. R. 673, 117 Fed. 1 (C. C. A. Mo.); *Doyle v. Milw. Nat. Bk.* (*In re Harpke*), 8 A. B. R. 535 (C. C. A. Wis.).

receive none of the bankrupt's property, there is no preference. And that is the primary difficulty with the complainant's case. The defendant bank received no property or money of the Newport Company. The Sheard Company as indorser of the note took up and paid its own funds therefor—funds in which the Newport Company had no interest whatever. It is true that the Sheard Company at the time it paid the note was indebted to the Newport Company [the bankrupt], but that in no sense made its funds the property of the latter. An unsecured creditor has no interest in his debtor's property until he has sequestered it. The money, which the defendant received belonged to the Sheard Company [the indorser], and not to the bankrupt. It follows, then, that there was no preference unless that which was actually done can be treated as the equivalent for something else. And that is the theory of the District Court. It is pointed out that, if the Newport Company [the bankrupt] had collected its claim from the Sheard Company [the indorser], and had itself paid the note, there would have been a transfer from the Newport Company [the bankrupt] to the bank. And it is said that it was merely a short cut for the Sheard Company to pay the note and charge the amount paid upon its account against the Newport Company—that the effect of the two transactions was the same. There would be much force in this argument if the Sheard Company stood in the transaction merely as a debtor of the Newport Company. It may well be that when a debtor with the approval of his creditor takes up the latter's note at a bank, and offsets the amount paid upon his debt, the payment to the bank will be treated as having been made by the creditor; the debtor being really his agent in the transaction. But that was not the situation here. The Sheard Company was the indorser of the note, and had pledged its own property as security therefor. In taking up the note and collateral it acted in its own behalf, and in no sense as the agent of the Newport Company. The note was not discharged. The Sheard Company as against the Newport Company became the holder instead of the bank. Upon no permissible theory in law or equity can it be said that the note was paid by the Newport Company. But it is further urged that the effect of the transaction was to appropriate certain assets of the Newport Company, to wit, its demand against the Sheard Company, to the payment of this note to the exclusion of other creditors. * * * But it cannot be conceded that the result claimed would follow. If the Sheard Company, knowing the Newport Company to be insolvent, acquired the note with a view to using it as a set-off or counterclaim against its debt, it could not legally do so. * * * [Section 68.] And, if the Sheard Company could not offset the note against the account * * * there was no transfer or appropriation of such account, and much less a preference. The debt could still be collected by the trustee of the bankrupt."

The creditor may prove his claim in full, and if his dividends together with the payments received from sureties or endorsers exceed the total amount due, he holds the excess for the benefit of the surety or endorser.⁵⁵

§ 1288½. Payment by Third Party Not Preference.—Of course, the payment of the bankrupt's debt by a third party, where no property of the bankrupt was transferred to such party, is not a preference: the third party simply becomes a creditor in place of the original creditor.

55. *Swarts v. Fourth Nat'l Bk.*, 8 A. B. R. 673, 117 Fed. 1 (C. C. A. Mo.).

In *re Kerlin*, 31 A. B. R. 12, 209 Fed. 42 (C. C. A. Ohio, reversing 30 A. B. R. 816): "The case then, in its last analysis, amounts only to a substitution of creditors of the alleged bankrupt, and with the result that the indebtedness involved in the transaction was greatly reduced. * * * It is helpful to bear in mind that the transaction did not deplete Kerlin's estate (*Continental*) Trust Co. *v.* Title Co., 229 U. S. 435, 30 A. B. R. 624; on the contrary, as already stated, the settlement reduced the indebtedness, and to that extent in effect increased the assets."

§ 1289. Payment, by Maker, of Note Discounted by Bankrupt.—Where a third person's note not belonging to the bankrupt is nevertheless discounted at the bank and placed in the bankrupt's account, the maker's payment of it when due does not constitute a preference; the bankrupt's estate is not depleted.⁵⁶

But if the insolvent fund is depleted by the payment or other transfer, it is a preference; as would be the case where a customer's paper is discounted; and this is so, although third parties bound as sureties for the same debt would have paid the debt anyway.⁵⁷

§ 1290. Depletion of Partnership Assets Where Partnership Not in Bankruptcy but Assets Being Administered in Bankruptcy of Member.—Where partnership property is being administered in the individual bankruptcy proceedings of one of the partners, a mortgage given by the partnership upon partnership property that would have operated as a preference as to partnership creditors had the partnership been in bankruptcy, will not be affected by the individual bankruptcy of the partner—the individual estate, which is the only bankrupt estate involved, has not been depleted.⁵⁸

§ 1291. Conversely, Depletion of Individual Estate Not Preference in Partnership Bankruptcy.—Liens upon the individual property of a member of a bankrupt partnership that would have been voidable had he been individually in bankruptcy, are not voidable where merely the partnership is in bankruptcy.⁵⁹

56. *Dressel v. North State Lumber Co.*, 9 A. B. R. 541, 107 Fed. 225 (D. C. N. Car.).

57. *Swarts v. Fourth Nat'l Bk.*, 8 A. B. R. 673, 117 Fed. 1 (C. C. A. Mo.).

58. *McNair v. McIntyre*, 7 A. B. R. 638, 113 Fed. 113 (C. C. A. N. C.), reversing *In re Sanderlin*, 6 A. B. R. 384. But compare, *In re Keller*, 6 A. B. R. 334, 109 Fed. 118 (D. C. Iowa), which was also a case where a partner on dissolution of partnership assumed firm debts and afterwards went into bankruptcy: a payment by the firm that would have been a preference had the firm been in bankruptcy was held to be a preference as to the bankrupt

partner. Compare, *Miller v. Acid & Fertilizer Co.*, 21 A. B. R. 416, 211 U. S. 496. Compare post, § 2265. Also, compare, same proposition under "Second Element of a Preference," post, § 1312½.

59. Compare post, §§ 2265, 2268¼. Impliedly, *In re Lehigh Lumber Co.*, 4 A. B. R. 221, 101 Fed. 216 (D. C. Pa.). Obiter, *Mayes v. Palmer*, 31 A. B. R. 225, 208 Fed. 97 (C. C. A. Mo.). But, for instance of depletion of individual estate where both firm and individuals in bankruptcy, see *Brewster v. Goff Lumber Co.*, 21 A. B. R. 106, 164 Fed. 124 (D. C. Pa.).

A transfer by one member of a partnership of his individual property, within four months of the bankruptcy of the partnership, is not a preference in the partnership bankruptcy.⁶⁰

Nevertheless, the property of the partner is *sub modo* a fund for firm creditors; and a transfer of it to a firm creditor may operate as an individual preference, for a firm creditor may prove against the individual estate.⁶¹

Mills v. Fisher & Co., 20 A. B. R. 237, 159 Fed. 897 (C. C. A. Tenn.): "There remains the question as to whether John H. Fisher can be individually adjudicated a bankrupt upon the averments of this petition. If we construe the averments to be that Fisher has applied his individual property to the payment of a joint debt, and we think we must, intending to prefer that debt over other firm debts, we are confronted with the question as to whether that is not a preference for which he may be adjudicated a bankrupt? He was individually liable for every partnership debt, as well as liable for his individual debts. In equity, and in bankruptcy, his individual creditors are entitled to be paid out of his individual property before his partnership creditors. Manifestly, if the claim of the Watts Mills is an individual debt against J. H. Fisher, there would be no doubt but that such a preference of one creditor over another of the same class would be an act justifying an adjudication in bankruptcy. That is too plain to need discussion. But that is not the case. The claim of the Watts Mills is against the firm and the preference was not given out of the firm property, but out of the separate property of J. H. Fisher. The utmost right of such a joint creditor against the individual assets of John H. Fisher was to share in them equally with other joint creditors after individual debts had been paid. If, therefore, the debt preferred was an individual debt, it was not a preference of which a partnership creditor can complain, for the debt paid was entitled to a preference over every partnership debt, including, of course, the petitioner's claim. A preference under § 60a of the Bankrupt Act is only such when it will enable any one of his creditors 'to obtain a greater percentage of his debt than any other of such creditors of the same class.' This is the principle upon which the payment of labor claims is not a preference; provided only that the general assets are enough to pay all other labor claims as great a percentage. * * * While the averments of the petition in respect to the character of the debt preferred are not as clear as they should be, we nevertheless regard the petition as resting the claim to an adjudication against J. H. Fisher upon the fact that he has transferred practically and substantially his entire separate estate, being insolvent at the time, in payment of a debt of the firm of J. H. Fisher and Company, intending to prefer that debt over other debts of the same class. It is no answer to say that partnership creditors are benefited and not injured by such an application of the individual property of one of the members. If the fact be as averred, that there were no joint or firm assets applicable to joint debts, and that neither of the partners had any separate property, other than that transferred to one of the joint creditors, it would seem that the one joint creditor had been very substantially preferred over every other creditor of the same class. That the members of the firm were each liable in *solido* for the joint debts is not disputable. Undoubtedly

60. Compare same proposition under "Second Element of a Preference," post, § 1312½; *obiter*, *Mills v. Fisher & Co.*, 20 A. B. R. 237 (C. C. A. Tenn.);

Miller v. Acid & Fertilizer Co., 21 A. B. R. 416, 211 U. S. 496.

61. See post, §§ 2268½, 1387½, 2268¼, ante, §§ 171, 217.

the individual creditors of John H. Fisher would be preferred over the joint creditors out of his individual estate. But if there were none, then the whole of that separate property would have been subject to the demands of the joint creditors. If there were such separate creditors, then the right of the joint creditors to the surplus, after paying the other class of debts, is not deniable. That this preference of the individual creditor exists independently of the existence of partnership assets under the Bankrupt Act of 1898, may be conceded upon the reasoning and authority of *In re Wilcox*, 2 Am. B. R. 117, 94 Fed. 84; *In re James*, 13 Am. B. R. 341, 133 Fed. 912; and *Euclid Nat. Bank v. Union Trust and Deposit Co.*, 17 Am. B. R. 834, 149 Fed. 975. Nevertheless, the right of a partnership creditor to share in the separate estate of the members of the co-partnership, gives him such an interest in the separate property of its members as to entitle him to prove his claim against the separate estate and to make such a claim the basis for an adjudication of bankruptcy against a member of a firm who has given a preference out of his estate. This was well settled under former acts and in this respect the present law has not changed the rule. *In re Melick*, Fed. Cas. No. 9,399; *In re Jewett*, Fed. Cas. No. 7,306; *In re Remond*, Fed. Cas. No. 11,632; *In re Loyd*, Fed. Cas. No. 8,429; *In re McLean*, Fed. Cas. No. 8,879; *Hartman v. Peters*, 17 Am. B. R. 61, 146 Fed. 82. Upon the facts stated in this petition it is obvious that when one member of a firm which is insolvent and without assets, applies his whole separate estate in satisfaction of one joint liability, that creditor will receive a greater percentage of his debt than other creditors of the same class. This, at last, is the supreme test of a preference."

§ 1292. Whether Liens upon or Other Transfers of Exempt Property, Preferences.—It has been held that liens upon or other transfers of exempt property do not constitute preferences, since they do not diminish the creditors' assets, title to exempt property not passing to the trustee.⁶²

But it has been held that, at any rate, where the property out of which the exemption is to come exceeds in value the exemption allowance, it may be administered in the bankruptcy court so that the excess may be available as an asset; and, therefore, that a transfer of partially exempt property may constitute a preference to the extent that its actual value exceeds the exemption.⁶³

⁶² See, analogously as to liens by legal proceedings on exempt property, § 1100, et seq.

Compare, obiter, *In re Tollett*, 5 A. B. R. 404, 106 Fed. 866 (C. C. A. Tenn.), wherein the court held that on recovery of property fraudulently or preferentially conveyed the debtor might have his exemptions therefrom, giving as one reason that since it was exempt it could not have depleted the estate anyway. Such argument, however, proceeds in a circle, for if the transfer did not deplete creditors' assets, then it was not fraudulent nor preferential, hence the property was

not recoverable by creditors. A better basis should be found than such argument, it would seem. Compare, also, *In re Leech*, 22 A. B. R. 599, 171 Fed. 622 (C. C. A. Ky.). Also, compare, § 1033½, note, and § 1095.

That creditors may not complain of transfers of exempt property as fraudulent, see ante, § 1224½.

Compare obiter, *In re Wishniefsky*, 24 A. B. R. 798, 181 Fed. 896 (D. C. N. J.); *Huntington v. Baskerville*, 27 A. B. R. 219, 192 Fed. 813 (C. C. A. S. D.).

⁶³ *First Nat. Bank v. Lanz*, 29 A. B. R. 247, 202 Fed. 117 (C. C. A. La.).

In *re Bailey*, 24 A. B. R. 201, 176 Fed. 990 (D. C. Utah): "A mortgage constituting an unlawful preference, where it includes both exempt and non-exempt property, is only voidable by the trustee as to the non-exempt property, and remains a valid mortgage as to the exempt property."

Compare, *obiter*, *Mills v. Fisher & Co.*, 20 A. B. R. 239, 159 Fed. 897 (C. C. A. Tenn.): "So the transfer of a homestead exemption is not a preference, since it is not subject to the demands of creditors."

Vitzthum v. Large, 20 A. B. R. 666, 162 Fed. 685 (D. C. Iowa): "If a part of the property transferred by the bankrupt to the bank was exempt, or the proceeds of exempt property, under the Iowa statute, the creditors generally would have no right thereto, nor the trustee, to recover the same for their benefit."

Contra, In *re Soper*, 22 A. B. R. 868, 173 Fed. 116 (D. C. Neb.): "The effect of the surrender of the preference [chattel mortgage on exempt and non-exempt property, which creditor claimed to be still good on the exempt property] was to restore the property of the bankrupt to his estate as if no mortgage had ever been made upon the property. The bankrupt has not lost his right to claim his exemptions unless it is because of the mortgage given by him. The trustee did not obtain the property under the mortgage, but in hostility to it. It came into his hands unburdened by the mortgage, and as if the mortgage had never been given. Therefore neither the trustee nor the bankrupt are estopped by the terms of the mortgage. From the time the trustee took the property until such time as the bankrupt should assert his claim of exemptions, the trustee had the title to all the property, and the mortgage was no lien upon any portion of it. Upon the assertion of the right of the bankrupt to his exemptions, the mortgage was not revived upon the articles selected as exempt."

So, it has been held that the payment of an encumbrance on exempt property within the four months period is not a voidable preference.⁶⁴

It is to be observed, at any rate, that if the questions of the exemptability of the property transferred and, consequently, of the preferential character of the transfer, are to be determined as of the date of each transfer, then the rule of the cases cited would afford a convenient means, by making successive transfers of exempt property, of actually perpetrating preferences with impunity. If each transfer be only small enough to come within the exemption right at the particular time, the entire estate might, by successive transfers, be distributed among a few favored creditors.

§ 1293. Transfers of or Liens on Property That Might Have Been Claimed Exempt but Not Claimed.—Transfers of, or liens upon property that might have been claimed as exempt but is not so claimed, are none the less on that account preferences.⁶⁵

§ 1294. Property Transferred to Be Such as Otherwise Would Have Belonged to Estate.—The property transferred must have been such as otherwise would have belonged to the bankrupt's estate, else there

⁶⁴. *Southern Irr. Co. v. Wharton Nat. Bank*, 28 A. B. R. 941 (Civ. App. Tex.).

⁶⁵. *Obiter*, In *re Schuller*, 6 A. B. R. 278, 108 Fed. 591 (D. C. Wis.).

can be no depletion of the trust fund.⁶⁶ Thus, although preferences may be given after the filing of the petition and before adjudication (§ 60a), yet they may only be accomplished as to property, or its proceeds, that was in existence at the time of the filing of the petition and that might then have been transferred by some means or levied on and sold under judicial process.

§ 1294 $\frac{1}{4}$. Release of Dower in Preferential Mortgage.—However, a release of dower by the bankrupt's wife in a mortgage to secure her husband's debt does not remain available to the mortgagee upon the setting aside of the mortgage as a preference, but this is so because a release of dower is only an incident to a conveyance of the estate by the owner, the release falling with the fall of the conveyance.⁶⁷

§ 1294 $\frac{1}{2}$. Property in Foreign Countries.—Doubtless, transfers of property in foreign countries could be preferences, though, if real estate, the only way to reach the case would probably be by such process as could operate on defendants or claimants found in this country, since the title could not pass by operation of law under § 70 (a).⁶⁸

§ 1295. Mere Exchanges of Property, Changes in Form and Transfers Based on Present Consideration, Not Preferences.—"A fair exchange is no robbery." Mere exchanges of property and changes in its form, as, likewise, transfers of it, for which are received at the same time assets of equal value, do not deplete the estate nor constitute a basis of preference.⁶⁹

City Nat'l Bk. of Greenville v. Bruce (Bank *v. Bruce*), 6 A. B. R. 311, 109 Fed. 69 (C. C. A. S. Car.): "This paragraph (§ 60 (a)) refers to existing debts as distinguished from a security or lien given upon the bankrupt estate to raise ready money whereby the value of the estate is increased to the extent of the amount raised."

66. In *re Leech*, 22 A. B. R. 599, 171 Fed. 622 (C. C. A. Ky.), quoted at § 1277; *National Bank of Newport v. National Herkimer Co. Bank*, 28 A. B. R. 218, 225 U. S. 178; In *re Kerlin*, 31 A. B. R. 12, 209 Fed. 42 (C. C. A. Ohio, reversing 30 A. B. R. 816), quoted at § 1288 $\frac{1}{2}$; In *re Martin* (*Goodwin v. Headley*), 29 A. B. R. 623, 200 Fed. 940 (C. C. A. N. J.).

Instance held not to be such property—insurance policy payable to estate where the bankrupt had previously borrowed from the company up to the extent of the cash surrender value. *Burlingham v. Crouse*, 24 A. B. R. 632, 181 Fed. 479 (C. C. A. N. Y., affirmed in 228 U. S. 459, 30 A. B. R. 6), discussed at §§ 1003, 1006, 1012.

Compare, analogous proposition that creditors may not complain of the transfer of exempt property as fraudulent, ante, § 1224 $\frac{1}{2}$.

67. In *re Lingafelter*, 24 A. B. R. 656, 181 Fed. 24 (C. C. A. Ohio).

68. Compare, § 1450 $\frac{1}{2}$; also see, analogously, In *re Pollman*, 19 A. B. R. 474, 156 Fed. 221 (D. C. N. Y.), quoted at § 1450 $\frac{1}{2}$.

69. In *re Cutting*, 16 A. B. R. 753, 148 Fed. 388 (D. C. N. Y.); *Cook v. Tullis*, 85 U. S. 332; In *re Reese-Hammond, etc., Co.*, 25 A. B. R. 323, 181 Fed. 641 (C. C. A. Pa.); In *re Crafts-Riordan Shoe Co.*, 26 A. B. R. 449, 185 Fed. 931 (D. C. Mass.); In *re Jackson, etc., Co.*, 26 A. B. R. 915, 189 Fed. 636 (D. Co. Mo.); [1867] *Stewart v. Hopkins*, 30 Ohio St. 531, quoted at § 1325. In *re Nicholas*, 10 A. B. R. 291 (D. C. N. Y.), in which case an exchange—under the terms of the bankrupt's contract—of old goods for new goods (eight old ones for seven new ones) was held not a preference. See post, "Third Element of Preference," § 1320.

In re Manning, 10 A. B. R. 503, 133 Fed. 180 (D. C. S. C.): "There is nothing in the Bankrupt Law which forbids an exchange of securities, and if a person, even while insolvent, makes such exchange as will not diminish the value of his estate, it is unimpeachable."

In re Shepherd, 6 A. B. R. 725 (D. C. Ills.): "The mere exchange of securities within four months is not a preference within the meaning of the Bankrupt Law; the reason being that the exchange takes nothing from the other creditors."

In re Clifford, 14 A. B. R. 283, 136 Fed. 475 (D. C. Iowa): "And for such part of the mortgage the bankrupt then received a present consideration, and his estate was not diminished nor the rights of any of his then existing creditors impaired in the least."

[1867] Sawyer v. Turpin, 91 U. S. 114: "The mortgage covered the same property. It embraced nothing more. It withdrew nothing from the control of the bankrupt, or from the reach of the bankrupt's creditors, that had not been withdrawn by the bill of sale. Giving the mortgage in lieu of the bill of sale, as was done, was therefore a mere exchange in the form of the security. In no sense can it be regarded as a new preference. The preference, if any, was obtained on the 15th of May, when the bill of sale was given, more than four months before the petition in bankruptcy was filed. It is too well settled to require discussion that an exchange of securities within the four months is not a fraudulent preference within the meaning of the bankrupt law, even when the creditor and the debtor know that the latter is insolvent, if the security given up is a valid one when the exchange is made, and if it be undoubtedly of equal value with the security substituted for it."

McDonald v. Clearwater R. Co., 21 A. B. R. 182, 164 Fed. 1007 (U. S. C. C. Idaho): "Property transferred by a borrower at the time of receiving a loan and for the purpose of making the lender safe, is security; its validity, if unaccompanied by positive fraud, is recognized and enforced in bankruptcy. Transfers which do not diminish the estate of the bankrupt, but which constitute only a fair exchange of property, are not preferences."

§ 1296. Net Result after Becoming Insolvent and within Four Months, the Test.—If the net result of the transactions between the debtor and creditor during the period of insolvency and within the four months of the bankruptcy has been to increase rather than to diminish the trust fund of the creditors, such creditor has not received a greater percentage of his claim out of the insolvent estate than some other creditor of the same class, and there is therefore no preference.⁷⁰

Jaquith v. Alden, 9 A. B. R. 776, 189 U. S. 78: "In the present case all the rubber was sold and delivered after the bankrupt's property had actually become insufficient to pay their debts, and their estate was increased in value thereby to an amount in excess of the payments made. The account was a running account, and the effect of the payments was to keep it alive by the extension of new credits, with the net result of a gain to the estate of \$546.89, and a loss

⁷⁰ In re King Co., 7 A. B. R. 619 (D. C. Mass., citing Jourdan-Dickson v. Wyman, 7 A. B. R. 186, 111 Fed. 726, C. C. A. Mass.); Morey Mercantile Co. v. Schiffer, 7 A. B. R. 670, 114 Fed. 447 (C. C. A. Colo.); In re Sagor & Bro., 9 A. B. R. 361, 121 Fed. 658 (C. C. A. N. Y.); Kimball v. Rosenbaum

Co., 7 A. B. R. 718, 114 Fed. 85 (C. C. A. Ark.). Impliedly, Wild & Co. v. Provident Life & Trust Co., 22 A. B. R. 109, 214 U. S. 292, quoted at § 1419. See further, as to this rule, post, subject of "Offsets of New Credits against Preferences," § 1419; also see "Eighth Element of a Preference," post, § 1386.

to the seller of that amount, less such dividends as the estate might pay. In these circumstances the payments were no more preferences than if the purchases had been for cash, and, as parts of one continuous bona fide transaction. The law does not demand the segregation of the purchases into independent items so as to create distinct pre-existing debts, thereby putting the seller in the same class as creditors already so situated, and impressing payments with the character of the acquisition of a greater percentage of a total indebtedness thus made up."

Gans v. Ellison, 8 A. B. R. 153, 114 Fed. 734 (C. C. A. Pa.): "Upon the true interpretation of paragraph 'a' of § 60, the preference in such case as this is the net gain to the creditor upon the transactions between him and the debtor. The net balance in favor of the creditor is the real preference under the law. For only to the extent of such net gain does the creditor 'obtain a greater percentage of his debt than any other creditors of the same class.' And so, on the other hand, only to the amount of the net gain to the creditor is the estate of the debtor impaired. If, then, a creditor innocently preferred has given return credits afterwards he has surrendered his preference to the extent of such return credits. To effectuate justice, both sides of the account are to be considered in the case of a creditor who innocently has received preferences, and afterwards in good faith has given the debtor further credit, without security, for property which has become a part of the debtor's estate. Otherwise it is plain that such innocently preferred creditor would be compelled to surrender his preference a second time before he could prove his claim against the bankrupt's estate." Although this case was decided as to "innocent" preferences, so-called, before the Amendment of 1903, the reasoning is still applicable.

Peterson v. Nash, 7 A. B. R. 181, 112 Fed. 311 (C. C. A. Minn.): "The giving and receiving, under such circumstances, may properly enough be regarded as one transaction, resulting not in a preferential payment to the creditor, but, in reality, in the creation of an indebtedness in favor of the creditor for the difference between the two."

In *re Geo. M. Hill Co.*, 12 A. B. R. 221, 120 Fed. 315 (C. C. A. Ills.): "We think that in stating the accounts between the parties, within the rule declared in *Jacquith v. Alden*, all the transactions between the parties must be included, and that we are not limited to an account as it is stated or was kept by the bank, because we are to inquire, whether the net result of the transaction was to increase or decrease the estate of the bankrupt. If the account was stated including that amount, there remains no question that the net result of the dealings was to decrease the bankrupt's estate, and that the bank is therefore chargeable with the amount of that net decrease as a condition of proving its claim."

§ 1297. Deposits in Bank Subject to Check.—Deposits in bank, subject to check and not made to apply in payment of a debt, are not preferences, though subsequently offset by the bank against a debt owed it by the depositor. The deposit creates a corresponding credit against which checks may be drawn—the estate is not depleted by the making of the deposit, and the subsequent offsetting by the bank does not constitute later a "transfer" by the bankrupt.⁷¹

71. See ante, § 1180. See post, this subdivision, "Fifth Element of Preference—Transfer," § 1341; *N. Y. County Nat. Bk. v. Massey*, 11 A. B. R. 42, 192 U. S. 138; In *re Philip Semmer*

Glass Co., L't'd, 14 A. B. R. 25, 135 Fed. 77 (C. C. A. N. Y., affirming 11 A. B. R. 665); In *re Geo. M. Hill Co.*, 12 A. B. R. 221, 120 Fed. 315 (C. C. A. Ills.); instance, In *re Medaris-*

West v. Bk. of Lahoma, 16 A. B. R. 738, 16 Okla. 508: "The Bank of Lahoma, as shown by the averments in the petition, loaned to Streich the sum of \$1,800, and Streich executed his promissory note to the bank for said amount. The bank gave him credit on deposit account for the proceeds of the loan. The bank then became his debtor to the amount of the deposit. He became the debtor to the bank in the amount of the note. The deposit was subject to check, and the transcript of account from the bank's books, which accompanies the petition as an exhibit, shows that the bank paid out on his check \$500 of the deposit before the note matured. On the date the note fell due Streich had on deposit of the original sum borrowed \$1,300, and the bank applied this sum on his note, and gave him credit for payment of that sum, and charged the same to him on the account. The deposit in the first instance did not create a preference in favor of the bank, for the reason that the bank became his debtor for the full amount of the deposit. His available assets were not diminished by the deposit in the bank, and his other creditors of the same class were in as good a position as they were before. These mutual transactions brought about the exact conditions mentioned in § 68a, a case of mutual debts and mutual credits between the estate of the bankrupt and the creditor, and after the adjudication the bank would have been entitled to have had set off the amount of Streich's deposit against the amount due on his note to the bank, and the right to have the balance allowed against the estate."

But, of course, if it was agreed that the subsequent deposits should be applied as they were made upon pre-existing overdrafts or other debts, then they would not constitute simply "offsets" but would amount to "preferences."⁷²

Compare, to this general effect, *In re Starkweather & Albert*, 30 A. B. R. 743, 206 Fed. 797 (D. C. Mo.): "While as held in the Massey case, money deposited with the bank in the ordinary course of business creates a relation of debtor and creditor, and while in that case it is held that money so deposited may be applied by the bank as a set-off against any indebtedness by the bankrupt to it, it is distinctly indicated by the Massey case that where a deposit is not made for general purposes, but for the purpose of creating a fund to be used in set-off, the privilege of set-off does not exist, and that the application of such money pursuant to such an arrangement is preferential."

And a deposit was held to constitute a preference where it appeared that the bank induced the making of it with the intention and for the purpose of applying it on an indebtedness owing to the bank by the depositor.⁷³ Thus, where a bank required a depositor to give it a check on his account

Vine Carriage Co., 17 A. B. R. 879 (Ref. Ohio); *In re Scherzer*, 12 A. B. R. 451, 130 Fed. 631 (D. C. Iowa); *Irish v. Citizens Trust Co.*, 21 A. B. R. 39 (D. C. N. Y.); *Booth v. Prette*, 22 A. B. R. 579, 81 Conn. 636, 71 Atl. 938; *Germania Savings & Trust Co. v. Loeb*, 26 A. B. R. 238, 188 Fed. 285 (C. C. A. Tenn.); *Studley v. Boylston Nat. Bank of Boston*, 29 A. B. R. 649, 200 Fed. 249 (C. C. A. Mass.), affirmed (229 U. S. 523, 30 A. B. R. 161); *Studley*

v. Boylston Nat. Bank, 225 U. S. 523, 30 A. B. R. 161, affirming (29 A. B. R. 649, 200 Fed. 249); *Trust & Savings Bank v. Trust Co.*, 229 U. S. 435, 30 A. B. R. 624.

⁷² *Obiter*, *Bank v. Sandheim*, 16 A. B. R. 866 (C. C. A. Penn.); *contra*, *obiter*, *Tomlinson v. Bk. of Lexington*, 16 A. B. R. 632 (C. C. A. N. Car.).

⁷³ *Schmidt v. Bank of Commerce*, 25 A. B. R. 904 (Sup. Ct. N. Mex.).

in payment of notes not then due, the transaction was held to constitute a preference.⁷⁴

Again, the right of offset has been refused where a deposit was made after the bank had ordered that no more certificates should be made, thereby closing the account and terminating the relation of debtor and creditor as to future transactions.

Ernst v. Mechanic's, etc., Bank, 29 A. B. R. 289, 201 Fed. 664 (C. C. A. N. Y.): "In the case of the Mechanics National Bank, a deposit was made by Fiske & Company on the morning of January 19, which the trustee claims should be returned with interest as a voidable preference. This for the reason that the bank had ordered no more certifications to be made before the deposit was received, which it is contended was a closing of the account, so that the relation of debtor and creditor between the firm and the bank did not exist as to this fund. The special master and the court below held that the deposit was made after the bank had knowledge of the broker's insolvency, or at least was put on inquiry, so that the deposit was a voidable preference, just as much as the delivery of the securities. In this view we concur."

Likewise they would amount to preferences if they were simply devices for obtaining payment of the bank's claim by indirect means.⁷⁵

Walsh v. First Nat. Bank, 29 A. B. R. 118, 201 Fed. 522 (C. C. A. Ky.): "The undisputed facts are that the Tiger Shoe Manufacturing Company, the bankrupt, was indebted to the First National Bank of Maysville, Kentucky, in the sum of \$2,000.00, with interest, evidenced by two promissory notes, in equal amounts, of date January 4, 1901, and June 9, 1901. The notes had matured. On or about September 24, 1901, the wife of the secretary and treasurer of the bankrupt loaned the bankrupt \$3,000 upon a mortgage given by it for \$5,000. The amount so loaned was deposited to the bankrupt's credit with the defendant bank, and the amount paid to the bank in satisfaction of the two notes for \$1,000 each, with interest, was paid by a check drawn by the secretary and treasurer of the bankrupt on the amount so deposited. The only question presented is as to whether or not the payment of the two notes is a voidable preference? In the absence of a collusion, fraud, or insolvency of the debtor, the bank had a right to apply so much of the deposit as was necessary to the payment of its debt. It did not need a check to enable it to get the money. *New York County Nat. Bank v. Massey*, 192 U. S. 138, 11 Am. B. R. 42, 24 Sup. Ct. 199, 48 L. Ed. 380; *Germania Savings Bank & Trust Co. v. Loeb* (C. C. A., 6th Cir.), 26 Am. B. R. 238, 188 Fed. 285, 110 C. C. A. 263. However, as was said by the court below, 'The real claim of the appellant is that Hopper (secretary and treasurer of the bankrupt), and his wife were acting in collusion with the defendant bank in order to enable it to get its money and not be subject to a suit to recover it back as a voidable preference.'"

And it has been held that checks deposited for collection on the same day, though shortly before the bankruptcy petition was filed, but not collected until the next day, may not be offset.

Moore v. Third National Bank of Phila., 24 A. B. R. 568 (Pa. Sup. Ct.): "The rule in bankruptcy, as in other judicial proceedings, is that as to the general

74. *Shale v. Farmers' Bank*, 25 A. B. R. 888 (Sup. Ct. Kan.). 75. See post, § 1300.

doctrine, the law does not allow fractions of a day and that such fractions will only be considered where substantial justice so requires. *Dutcher v. Wright*, 94 U. S. 553; *Taylor v. Brown*, 147 U. S. 64. The deposit of these checks was not a deposit of money; the bank took the checks for collection, it advanced no money upon them, and parted with nothing upon the faith of the deposit. It was not a holder of checks for value. *National Bank v. Bonsor*, 38 Pa. Sup. Ct. 275."

However, the Supreme Court has held that the bank's right of offset of a deposit against the customer's notes is not vitiated nor converted into a preference by the intentional giving of checks thereon to pay the notes within the four months prior to the bankruptcy, holding that this was not a voluntary preference, but a voluntary offsetting;⁷⁶ but it is difficult to see what the checks amounted to if not a voluntary transfer; otherwise the giving of them was without significance.

§ 1298. Surplus of Collateral Applied by Pledgee on Other Claims.—Where the lienholder appropriates the equity and applies it to another and pre-existing debt, as by selling the security, for more than the debt secured and applying the surplus on another debt, the appropriation of the equity by virtue of a "banker's lien" constitutes a preference,⁷⁷ the lien being in the contemplation of both parties at the time of the pledging.

§ 1299. Any Kind of Property May Be Subject to Preference.—Any kind of transferable property may be the subject of a preferential transfer, so long as it depletes the estate.⁷⁸ Thus, the transfer of accounts receivable may constitute a preference.⁷⁹

As noted, ante, § 1280, the performance of labor in payment of a debt is not a transfer of property nor does it deplete the estate.

§ 1300. Any Method of Depleting Assets, Sufficient: Indirect Preferences.—Any method of depleting the insolvent fund is sufficient: a preference may be accomplished indirectly.⁸⁰

Bank of Newport v. Herkimer Co. Bank, 225 U. S. 178, 28 A. B. R. 218: "To constitute a preference, it is not necessary that the transfer be made di-

^{76.} Compare discussions, post, §§ 1329 and 1341.

^{77.} Inferentially, *In re Belding*, 8 A. B. R. 718 (D. C. Mass.). To same effect, see *Johnson v. Hanley, Hoyer Co.*, 26 A. B. R. 748, 188 Fed. 752 (D. C. R. I.), quoted at § 1300. See post, § 1372.

^{78.} *Stern, Falk & Co. v. Trust Co.*, 7 A. B. R. 305, 112 Fed. 501 (C. C. A. Ky.). Instance, *Troy Wagon Wks. v. Vastbinder*, 12 A. B. R. 352, 130 Fed. 232 (D. C. Penn.): Transfer of notes given to bankrupt on sale of goods falsely claimed by him to have been left on consignment.

Instance, *Dickinson v. Security Bk. of Richmond*, 6 A. B. R. 551 (C. C. A. Va.): Return of note of third person

transferred to creditor to apply on bankrupt's debt.

^{79.} *National Bank of Newport v. National Herkimer Co. Bank*, 225 U. S. 178, 28 A. B. R. 218, quoted at § 1300.

^{80.} Compare, to same effect, but relative to act of bankruptcy, *In re McGee*, 5 A. B. R. 262, 105 Fed. 895 (D. C. N. Y.). Compare, to same effect, but relative to act of bankruptcy, *Goldman v. Smith*, 1 A. B. R. 266, 93 Fed. 182 (D. C. Ky.).

Instance, *Mason v. Nat. Herk Co. Bk.*, 21 A. B. R. 98, 163 Fed. 920 (D. C. N. Y.); instance, *Pratt v. Columbia Bk.*, 18 A. B. R. 406, 157 Fed. 137 (D. C. N. Y.); *In re Harrison Bros.*, 28 A. B. R. 684, 197 Fed. 320 (D. C. Pa.); obiter,

rectly to the creditor. It may be made to another, for his benefit. If the bankrupt has made a transfer of his property, the effect of which is to enable one of his creditors to obtain a greater percentage of his debts than another creditor of the same class, circuitry of arrangement will not avail to save it.

"It is not the mere form or method of the transaction that the act condemns, but the appropriation by the insolvent debtor of a portion of his property to the payment of a creditor's claim, so that thereby the estate is depleted and the creditor obtains an advantage over other creditors. The 'account receivable' of the debtor, that is, the amounts owing to him on open account, are, of course, as susceptible of preferential disposition as other property; and if an insolvent debtor arranges to pay a favored creditor through the disposition of such an account, to the depletion of his estate, it must be regarded as equally a preference, whether he procures the payment to be made on his behalf by the debtor in the account—the same to constitute a payment in whole or part of the latter's debt—or he collects the amount and pays it over to his creditor directly. This implies that, in the former case, the debtor in the account, for the purpose of the preferential payment, is acting as the representative of the insolvent, and is simply complying with the directions of the latter in paying the money to his creditor."

In *re Shantz & Son Co.*, 30 A. B. R. 552, 205 Fed. 425 (D. C. N. Y.): "The record shows that the president of the company during a period of financial stress conceived the plan of selling a part of its machinery—a part which was not in use, and the sale of which, it was thought, would not injure the business. It was his intention to start, with the consent of the purchasers of such machinery, a separate and independent plant; * * * The general scheme, as shown by the evidence, was to induce various creditors of the company to provide funds with which to buy such machinery, and to require them to pay their subscriptions only in case their debts against the company were fully satisfied; the agreement specifically providing that the subscribers were to buy the machinery only in case a sum equal to their subscriptions was first paid to them. This scheme appears so palpably to favor the creditors in question that the presumption at once arises that all the parties had reasonable cause to believe that they were receiving a preference over other general creditors. It is consequently difficult to avoid the conclusion that the plan adopted by the bankrupt company was a device to give certain creditors a preference over other creditors of the same class, and that the petitioning creditors were aware of such intention, and of the intention of the president of the bankrupt company to save as much as possible from the financial wreck and continue the business, notwithstanding the pendency of bankruptcy proceedings."

Johnson v. Hanley, Hoyer Co., 26 A. B. R. 748, 188 Fed. 752 (D. C. R. I.): "Upon the foreclosure of a mortgage upon firm property, there remained after satisfaction of the mortgage debt a considerable surplus belonging to the bankrupt firm. One of the copartners directed the mortgagee to pay from the surplus in his hands a debt due the defendant, a creditor, thereby creating a preference. In legal effect this transaction was the same as a direct payment by the firm to prefer a firm creditor."

In *re Federal Biscuit Co.*, 29 A. B. R. 393, 203 Fed. 37 (C. C. A. N. Y.); *Huntington v. Baskerville*, 27 A. B. R. 219, 192 Fed. 813 (C. C. A. S. D.); *Wickwire v. Webster, etc., Bank*, 27 A. B. R. 157 (Sup. Ct. Ia.); *Morris v. Tannenbaum*, 26 A. B. R. 368 (Ref. N. Y.).

Instance (Bankrupt owing a bank,

gives a chattel mortgage to secure the purchase price of a stock of merchandise which he buys from one who also owes the same bank: bank insists on transfer of mortgage to itself to secure both debts). In *re McDonald & Sons*, 24 A. B. R. 446, 178 Fed. 487 (D. C. S. Car.).

Thus the assignment of accounts by an insolvent corporation to one of its officers in payment of an antecedent debt constitutes a preference.⁸¹ Thus, the preference may be made to another for the benefit of the creditor.⁸² As, by a transfer through a dummy.⁸³

In re Beerman, 7 A. B. R. 431, 434, 112 Fed. 663 (D. C. Ga.): "If transactions of this sort are to be permitted, then, instead of a creditor taking a mortgage himself, when a debtor is in failing circumstances, he will get some one else to advance the money, agreeing that the person advancing the money shall suffer no loss, and thereby obtain by indirection a preference which he would be unable to get if he had acted directly with the debtor."

Crooks v. Bank, 3 A. B. R. 242, 46 N. Y. App. Div. 339: "It is the result or effect of the act done which is declared against, not the manner nor method by which it is done. No matter how circuitous the method may be if the effect of the transfer of property, etc."

§ 1301. Purchaser from Bankrupt Using Purchase Price to Pay Off Preferential Liens.—Thus, where the purchaser of the bankrupt's real estate uses the purchase price in paying off judgment liens suffered within the four months, he depletes the estate thereby and causes a preference.

Benjamin v. Chandler, 15 A. B. R. 443, 142 Fed. 242 (D. C. Pa.): "It does not matter that the bankrupt does not himself pay it. That is not to be expected from a failing debtor, and might never in consequence be realized. Neither does execution have to be issued. The lien obtained by virtue of the judgment, whereby payment is secured out of the property, is a sufficient enforcement of it within the meaning of the law. Neither does it change the character of the transaction, that payment is made by a purchaser from the bankrupt who appropriates the price he was to pay in clearing off the liens, in order to have an unencumbered title. The significant thing is, that, by virtue of the judgment which was given him for his debt, the creditor is paid out of the property of the bankrupt, while others not so favored have to wait. There can be no question that, if this was effected through the medium of a sheriff's sale, it would amount to a preference, and there is no essential difference that the sale is private. Otherwise, by a mere disposition of his property to a third party, after covering it with judgments, a failing debtor could prefer and make them all good. The law permits no such evasion of its terms. The payment of a judgment, secured in this way, is as much an enforcement of it as if execution issued and levy were made. By whomever paid, it comes out of the property of the bankrupt, against which it is a lien, and that is enough."

§ 1301½. Or to Pay Off Bankrupt's Debt.—Likewise, where the purchaser from the bankrupt, as part of the consideration, pays off a debt owed by the bankrupt to another creditor, it may be a preference.⁸⁴

^{81.} In re Richards, 28 A. B. R. 636 (Sup. Ct. Dist. Columbia).

^{82.} National Bank of Newport v. National Herkimer Company Bank, 28 A. B. R. 218, 225 U. S. 178.

^{83.} Morris v. Tannenbaum, 26 A. B. R. 368 (Ref. N. Y.).

^{84.} Rogers v. Fidelity Sav. Bank & Loan Co., 23 A. B. R. 1, 172 Fed. 735 (D. C. Ark.); Opp v. Hakes, 15 A. B. R. 696, 142 Fed. 364 (C. C. A. Ills.); Wickwire v. Webster City Savings Bank, 27 A. B. R. 157 (Sup. Ct. Iowa).

§ 1301 $\frac{1}{2}$. Proceeds of Mortgages, etc., Used to Make Preferences.

—It has been held that a mortgage given for money with which to make preferences is voidable as a preference, though given for presently passing consideration, if the mortgagee be cognizant of the purpose.⁸⁵

Walters v. Zimmerman, 30 A. B. R. 776, 208 Fed. 62, also 30 A. B. R. 780, 208 Fed. 62 (D. C. Ohio): "It is well suggested that, to permit these mortgages to stand, made as they are to a person who has at least constructive knowledge of the insolvency of the mortgagor and who is the executive officer and head of the creditor who obtains a preference, would be to furnish an easy opportunity to avoid the provisions of section 60 of the act."

Such was held to be the case where an insolvent debtor, on the eve of the bankruptcy, gave a mortgage on all his assets for a loan from a third party, giving a demand note therefor, the money then being deposited in a bank which was the largest creditor and which had acted as the lender's agent in the transaction.⁸⁶

Likewise, it has been held that a creditor, instrumental in effecting a sale of the bankrupt's business, who procures the assumption of his own debt by the purchaser as part of the transaction, receives an indirect preference.⁸⁷

Taking a mortgage made by the bankrupt to another debtor of the same creditor may be an indirect preference, though such mortgage be given in part for the purchase price of a stock of goods bought by the bankrupt from the other debtor.⁸⁸

But the fact that the mortgagee knew the proceeds were to be used in paying off existing creditors does not, in and of itself, make the mortgage void.⁸⁹

§ 1302. Return of Goods to Seller Where No Right of Rescission Exists, Preference.

—Thus, the return of goods to the seller on account of the buyer's insolvency, will constitute a preference, if title had actually passed and no right of rescission existed;⁹⁰ but will not be a preference if the right to rescind the sale for fraud exists.

Silberstein v. Stahl, 4 A. B. R. 626 (N. Y. Sup. Ct.): "The bankrupt law of 1898 would be very ineffective to protect the rights of creditors generally, and

⁸⁵. In *re Beerman*, 7 A. B. R. 431, 112 Fed. 663 (D. C. Ga.).

⁸⁶. In *re Lynden Mercantile Co.*, 19 A. B. R. 444, 156 Fed. 713 (D. C. Wash.).

⁸⁷. *Opp v. Hakes*, 15 A. B. R. 696, 142 Fed. 364 (C. C. A. Ill.); In *re Beerman*, 7 A. B. R. 431, 112 Fed. 663 (D. C. Ga.). Compare post, § 1504.

⁸⁸. In *re McDonald & Sons*, 24 A. B. R. 446, 178 Fed. 487 (D. C. S. Car.).

The deed of real estate by the bankrupt to an accommodation endorser, out of the proceeds of which the note was paid, has been held a preference. *Lazarus v. Egan*, 30 A. B. R. 287, 206 Fed. 518 (D. C. Pa.).

⁸⁹. *Stedman v. Bank of Munroe*, 9 A. B. R. 4, 117 Fed. 237 (C. C. A.); In *re Soudan Mfg. Co.*, 8 A. B. R. 45, 113 Fed. 804 (C. C. A.); In *re Kullberg*, 23 A. B. R. 758, 176 Fed. 585 (D. C. Minn.). Compare, In *re Pease*, 12 A. B. R. 66, 129 Fed. 446 (D. C.).

⁹⁰. Inferentially, *Lumber Co. v. Taylor*, 14 A. B. R. 231, 137 Fed. 321 (C. C. A. Penn.); *Plummer v. Myers*, 14 A. B. R. 805, 137 Fed. 660 (D. C. Penn.); impliedly, *Silvey & Co. v. Tift*, 17 A. B. R. 9, 123 Ga. 804. Also see post, § 1307. As to pleadings in such cases, see post, "Pleadings in Action to Recover Preferences," § 1761, et seq.

secure equality of distribution of the assets of an insolvent debtor, if each creditor who was lucky enough to find some of his goods on hand could take them, thus disposing of all the stock which was available for payment of any debts, and leaving the creditors whose merchandise had been entirely parted with by the debtor wholly unprotected; it would be equally as ineffective if the insolvent debtor could transfer his property to favored creditors, under the claim that the trustee took no title to such property."

§ 1303. Transfers to Indemnify Sureties and Other Indirect Preferences.⁹¹—Transfers to indemnify sureties may be an indirect means

91. Other Instances of Indirect Preferences.—1. Transfer of notes taken on resale by bankrupt of goods claimed to have been left on consignment, but in reality not left on consignment but sold to him originally. *Troy Wagon Wks. v. Vastbinder*, 12 A. B. R. 352, 130 Fed. 232 (D. C. Penn.).

2. Purchaser from bankrupt using purchase price to pay off judgment lien suffered thereon within the four months. *Benjamin v. Chandler*, 15 A. B. R. 443, 142 Fed. 242 (D. C. Penn.).

3. Creditor, instrumental in effecting sale of bankrupt's business procuring assumption of his own debt by purchaser as part of the transaction, receives an indirect preference. *Opp v. Hakes*, 15 A. B. R. 696, 142 Fed. 364 (C. C. A. Ills.).

4. Return of goods to seller on pretended rescission of sale by seller where no right of rescission exists. *Silberstein v. Stahl*, 4 A. B. R. 626 (N. Y. Sup. Ct.); inferentially, *Lumber Co. v. Taylor*, 14 A. B. R. 231, 137 Fed. 321 (C. C. A. Penn.).

5. General assignment for benefit of those creditors only who assent thereto. *In re Harson Co.*, 11 A. B. R. 514 (D. C. R. I.).

6. Giving orders on third person in payment of a pre-existing debt may be a preference. *In re Dundas*, 7 A. B. R. 129, 111 Fed. 500 (D. C. Vt.); *In re Hines*, 16 A. B. R. 495, 144 Fed. 142 (D. C. Penn.).

7. Transfer to liquidator to pay all creditors assenting to the liquidation is a preference to those assenting. *In re Wertheimer*, 6 A. B. R. 187 (Ref. N. Y.); *In re Wertheimer*, 6 A. B. R. 756 (D. C. N. Y.).

8. Leasing to a creditor a manufacturing establishment to pay himself from the profits of operation. *Carter v. Goodykoontz*, 2 A. B. R. 224, 94 Fed. 108 (D. C. Ind.).

9. Assignment of claim tainted with a preference to the purchaser of the bankrupt's assets for use as offset to the purchase price, under arrangement whereby such purchaser offers to sat-

isfy such account and assume such liability, contingent upon the purchase of the bankrupt's property, and the purchaser reserves from the purchase price an amount sufficient to satisfy the same. *Hackney v. Hargreaves Bros.*, 13 A. B. R. 164, 3 Neb. 676 (reversing *Hackney v. Raymond Bros. Clarke Co.*, 10 A. B. R. 213).

10. Transfer to any one who had guaranteed overdrafts of the bankrupt and had subsequently paid the overdrafts. This was, however, a case of a preference as an act of bankruptcy, not as a recoverable preference. *Goldman v. Smith*, 1 A. B. R. 266, 93 Fed. 182 (D. C. Ky.).

11. Clearing house association is the agent of each constituent bank, such that on recalling the checks presented by the bankrupt bank on the day of its failure it holds the resultant fund for the benefit of all and cannot appropriate it to the use of any particular creditor bank. *Rector v. City Deposit Bk. Co.*, 15 A. B. R. 336, 200 U. S. 405.

12. Payment of rent as part of a device to prefer. *In re Lange*, 3 A. B. R. 231, 97 Fed. 197 (D. C. N. Y.): "Payment of rent for leased premises where business is carried on is not usually a preference, but circumstances may render it such. * * * This will be the case where * * * the rent was paid for the purpose of continuing the business and that new debts were incurred, but that the proceeds of the business were not applied to the payment of debts, but were secreted by the alleged bankrupt." This case, however, exhibits rather a fraudulent scheme than a preferential payment.

12a. Bank owed at the same time both by bankrupt and by a third person from whom the bankrupt has purchased a stock of merchandise, receives as security for both debts, a chattel mortgage made by the bankrupt to such third person to secure the unpaid purchase price. *In re Mc-*

of making a preference;⁹² thus, an assignment of money due on a building contract as indemnity to an accommodation indorser may be a preference.⁹³

Likewise, the setting apart and marking of goods as security to an accommodation endorser or maker of a promissory note may be a preference.⁹⁴

Similarly, the taking of judgment on a judgment note given to a surety on a government contract for money advanced the same day to pay the pay roll has been held a preference,⁹⁵ though it would seem to have been based on a substantially presently passing consideration.

Donald & Sons, 24 A. B. R. 446, 178 Fed. 487 (D. C. S. Car.).

13. Mortgage on all assets of insolvent debtor given within four months, for a present loan, a demand note being given and the money being deposited in a bank which was the largest creditor, and which acted as the lender's agent, is a preference to the bank. In re Lynden Mercantile Co., 19 A. B. R. 444, 156 Fed. 713 (D. C. Wash.).

14. Accommodation endorser induces bankrupt to discharge obligation, real estate being transferred to the surety by the bankrupt out of the proceeds of which the note was paid. Lazarus v. Egan, 30 A. B. R. 287, 206 Fed. 518 (D. C. Pa.).

Other instances, claimed to be indirect preferences, but held not to be such:

1. Bankrupt removed from trusteeship on account of defalcation; ordered by court to make good the defalcation; transfers his store stock to wife who mortgages same and also her own property to raise the money to save husband from disgrace; held not a preference because person to whom payment was made was not a creditor. Fry v. Pennsylvania Trust Co., 5 A. B. R. 51 (Sup. Ct. Penn.).

2. Insolvent debtor giving his attorney money to effectuate a preference but attorney giving his own check to the creditor for sum in excess. Upson v. Mt. Morris Bk., 14 A. B. R. 6 (N. Y. Sup. Ct. App. Div.).

3. Construction Co. by arrangement with a storekeeper deducting amounts of supplies furnished laborers, out of pay roll, and sending check for same to storekeeper, suddenly stops sending checks to the storekeeper although still deducting from wages enough to pay for the supplies; held, an offset and not a preference. Western Tie & Timber Co., 13 A. B. R. 447, 196 U. S. 502, reversing 12 A. B. R. 111 (C. A. Ark.).

4. One partner selling out to the other who thereupon goes into bankruptcy, attempting thereby to convert from assets into individual assets; held, not a preference to individual creditor but, rather, that individual creditors are not entitled to share in old firm assets until firm creditors are satisfied, being a case of marshaling partnership and individual estates under Sec. 5 and not a case of preference under § 60. In re Denning, 8 A. B. R. 136, 114 Fed. 219 (D. C. Mass.).

5. Stockbroker turning over stock to customer on latter paying up; held no diminution of stockbroker's estate because customer owned stock and simply redeemed from the broker's lien. Richardson v. Shaw, 16 A. B. R. 842, 147 Fed. 659 (C. C. A. N. Y., affirmed in 16 A. B. R. 376); Richardson v. Shaw, 16 A. B. R. 876 (D. C. N. Y., affirming 16 A. B. R. 842).

6. Note of bankrupt paid by endorser, who released collateral which he had given to the creditor at the time of endorsement, not an indirect preference to the creditor receiving the payment notwithstanding endorser indebted to bankrupt and claims right to offset the right of indemnity against the bankrupt's claim. Mason v. Herkimer Co. Nat. Bank, 22 A. B. R. 733, 172 Fed. 529 (C. C. A. N. Y., reversing 21 A. B. R. 98, 163 Fed. 920).

7. Surrender by bankrupt father of daughter's note, their mutual debts being about equal. Taylor, trustee, v. Nichols, 23 A. B. R. 306, 134 App. Div. (N. Y.) 783.

92. Crandall v. Coates, 13 A. B. R. 712, 133 Fed. 965 (D. C. Iowa); In re Bailey & Son, 21 A. B. R. 911, 166 Fed. 982 (D. C. Pa.).

93. In re O'Donnell, 12 A. B. R. 621, 131 Fed. 150 (D. C. Mass.).

94. In re Bailey & Son, 21 A. B. R. 911, 166 Fed. 982 (D. C. Pa.).

95. Richardson v. Shaw, 209 U. S. 365, 19 A. B. R. 717; United Surety

§ 1304. Second Element of a Preference—The Claim upon Which the Preferential Transfer Is Made Must Have Been the Claim of a Creditor—Preference Implies Advantage Accruing by the Transfer to a “Creditor.”

In *re Kayser* (ex parte Weisbrod & Hess), 24 A. B. R. 174, 177 Fed. 383 (C. C. A. N. J.): “As we think, one requirement of this definition has not been met by the foregoing facts. It is true that the bankrupt was insolvent when the \$2,600 was paid. It is also true that the money was his, and that the effect of paying it to Weisbrod & Hess will be to reduce the percentage that would otherwise be paid to the petitioning creditor; but it is not true that Weisbrod & Hess were creditors of the bankrupt. On the contrary, the undisputed testimony shows that they were creditors of his wife, and that the loans upon which the \$2,600 was paid and credited were made to her and upon the credit of her separate property. In this essential particular the facts do not fit the statutory definition of a preferred creditor.”

§ 1305. Preferential Transfer to Be Distinguished from Fraudulent Transfer.—If the claim is fraudulent or fictitious, the transfer is not a preference but is a fraudulent transfer.⁹⁶ And an apparently merely preferential transfer may be shown to be in reality a fraudulent transfer by proof of the existence of a secret trust in the bankrupt's favor.⁹⁷

§ 1306. Paying Off Liens on Exempt Property—When Not Preference.—Paying off liens on exempt property within four months of bankruptcy, while the debtor is insolvent or otherwise converting nonexempt property into exempt property, will not entitle creditors to subrogation to the liens. The one receiving with knowledge the benefit, is not a creditor but is the bankrupt himself.⁹⁸

§ 1307. Return of Goods to Seller Where Right of Rescission Exists, Not Preference.—Where a seller has the right to rescind a sale and recover the goods, such right being predicated upon the failure of the title to pass for lack of meeting of minds, a return of such goods will not constitute a preference; for the seller thereby is declared never to have been a creditor for the goods and title to them is not in the bankrupt.

Co. v. Iowa Mfg. Co., 24 A. B. R. 726, 179 Fed. 55 (C. C. A. Mo.). Compare also, as to government contracts, post, § 2189.

^{96.} See ante, §§ 113, 1221; post, § 1397.

Transfer to Preferred Stockholders of Bankrupt Corporation—Preferred Stockholders Are Not Creditors.—Preferred stockholders are not creditors of the corporation and a transfer of the assets to secure them at the expense of creditors is void as against public policy. *Spencer v. Smith*, 29 A. B. R. 120, 201 Fed. 647 (C. C. A. Colo.), though not a “pref-

erence” within the meaning of the Bankruptcy Act.

Insolvent Corporation Giving Trust Deed to Secure Preferred Stockholders, Void as against Public Policy, Though Preferred Stockholders Not Being Creditors, It Is Not a “Preference.”—*Spencer v. Smith*, 29 A. B. R. 120, 201 Fed. 647 (C. C. A. Colo.).

^{97.} (*Van Iderstine*) trustee, *v. Nat'l Discount Co.*, 23 A. B. R. 345, 174 Fed. 518 (C. C. A. N. Y.).

^{98.} Apparently, *In re Wilson*, 10 A. B. R. 524, 123 Fed. 20 (C. C. A. Calif.); contra, *In re Boston*, 3 A. B. R. 388 (D. C. Neb.).

But of course, where such right did not exist, the return of the goods would constitute a preference.⁹⁹

§ 1307¼. Return of Goods to Bailor, Not Preference.—Of course the return of bailed goods to the bailor can not be a preference, for the relation of debtor and creditor does not exist.¹

§ 1307½. Payment for Property or Money Converted, Preference.—But the payment for goods wrongfully converted by the bankrupt—not the mere return of the same goods in specie—is a payment upon a provable debt and may constitute a preference.²

Likewise where the bankrupt as a guardian has embezzled funds of his ward, his making good of the defalcation by transfers from his individual estate, is a preference.³

Clarke v. Rogers, 228 U. S. 534, 30 A. B. R. 39, affirming 26 A. B. R. 413, 183 Fed. 518: "The criticism only can be made by putting out of view what the 'one embezzler' represents. He is one being but acts in more than one capacity, and in all of his capacities he has duties and obligations. The relation of a trustee to the trust property is not the same as his relation to his individual property. He certainly may incur obligations to the trust. He can only satisfy the obligations out of his individual property, and by doing so may deplete it, make it deficient, to satisfy its obligations." [This case is quoted further at § 1313 4-10.]

Similarly, the acceptance of a transfer of other property in specie to make good a conversion of funds, is an election to treat the conversion as a debt, and such payment may then be a preference; as, for example, a mortgage to cover a misappropriation of funds by an agent,⁴ or a transfer of real estate to make good a conversion of the proceeds of a note collected by the bankrupt for another.

Atherton v. Green, 24 A. B. R. 650, 179 Fed. 806 (C. C. A. Ills.): "So, the proceeds of the collection belonged to the principals, and the misappropriation vested no right to the fund in favor of the estate in bankruptcy, and the owner in such case is entitled to follow and recover the amount, in so far as it either remains on hand or is traceable into other investments or property derived therefrom. Failing such recourse to the trust fund, it is optional with the owner to treat the misappropriation as an indebtedness, thereby becoming a creditor on a par with other general creditors of the estate and subject to the bankruptcy provisions applicable to such relation. With neither the property nor its pro-

99. See ante, § 1302.

1. Compare, cases cited ante, under § 1228; also, see ante, § 1286½. Also, see *Walther v. Williams Mercantile Co.*, 22 A. B. R. 328, 169 Fed. 270 (C. C. A. Mich.), wherein the bailment of an entire business was upheld and the bailors' repossessing themselves of it held not a preference.

2. Impliedly, *Clingman v. Miller*, 20 A. B. R. 360, 160 Fed. 326 (C. C. A. Kans.). Compare, "Embezzlement

from Bankrupt Corporation," § 1333½.

Mistake of counsel causing mortgagee to relinquish rights of ownership and to claim simply as creditor for goods converted. In *re Strobel*, 20 A. B. R. 754, 163 Fed. 380 (D. C. N. Y.).

3. *Clarke v. Rogers*, 26 A. B. R. 413, 183 Fed. 518 (C. C. A. Mass.), quoted at §§ 635, 1308.

4. *Burgoyne v. McKillip*, 25 A. B. R. 387, 182 Fed. 452 (C. C. A. Neb.).

ceeds appearing on hand in any form, the fact that the indebtedness arose through conversion of the property gives the owner thereof no right of preference over general creditors."

The making good of a defalcation, however, has been held not to be a preference;⁵ yet, the claim on the defalcation certainly was a provable debt for the tort was waivable and the claim could have been presented *ex contractu*.⁶

It has been held that where the bankrupt's employees stole flour, which was on deposit for the bankrupt and others with a warehouse, payments and transfers of property by the bankrupt to the warehouse company to make good the shortage, which the warehouse company had in turn made good to its depositors, was not a preference, since the warehouse company was not a creditor of the bankrupt, being liable, if at all, simply for negligence.

Keystone Co. v. Bissell, 30 A. B. R. 213, 203 Fed. 652 (C. C. A. N. Y.): "This section [Bankruptcy Act, § 60 (a) (b)] plainly contemplates that the person to whom the transfer is made is one to whom, at the time, the bankrupt is liable. * * * We are unable to see how the repeated thefts of flour from the compartments of the defendant's warehouse, without any knowledge on its part of the thefts, made it a creditor of the Milling Company. There is a vital distinction between this case and that of *Atherton v. Green* and similar cases. In the *Atherton* case, the note which Green sent to the banker, who converted its proceeds, was the property of Green; the stolen flour was not the property of the Warehouse Company. The shipper (or the bank) owned the flour, and the Warehouse Company was merely a custodian or bailee, to keep it safe for the owner until the purchaser paid for it. It is true that the Warehouse Company could have sued for the stolen flour—its possessory title as bailee gave it the right to do so; but in such action it would sue merely as the trustee for the owner and was bound to turn over the proceeds of such suit, less its own charges against the owner, to such owner."

"The bank, as holder of the bill of lading, could have sued the Milling Company directly. It could also have brought an independent suit against the Warehouse Company for negligent care of the flour, in which suit it could recover only upon proof of negligence, and might have been defeated by some proof of acquiescence on its part in the Warehouse Company's methods of protecting the stored goods. But that is an independent action, the issues of which are not properly presented in the suit at bar, to which the bank is not a party, and by the decision of which it will not be bound. The circumstances that the bank might maintain an independent suit against its bailee does not alter the legal relations of the Milling Company and the Warehouse Company. The Milling Company bought the flour from the shipper, and whether it got possession of the flour with the latter's consent, or against it, by stealing it from the latter's custodian, it was the debtor solely of the shipper (or the bank) until the flour was paid for. This action is not brought against the creditor, shipper, or bank, to set aside a transfer of property to him or it.

5. *Fry v. Penn Trust Co.*, 5 A. B. R. 51. Compare, *McNaboe v. Columbian Mfg. Co.*, 18 A. B. R. 684, 153 Fed. 967 (C. C. A. N. Y.).

6. See ante, § 636, and post under subject of "Discharge," § 2733.

On the contrary, the trustee is seeking to recover the value of the property transferred to the Warehouse Company as collateral to the Milling Company's note to it, as if the Warehouse Company had been a creditor of the Milling Company before this note was made. We think it was not such creditor, and that, there being no antecedent liability, the trustee was not entitled to recover."

But, if the fund or property itself is traced and returned in its changed form, in accordance with the rules of equity governing the tracing of trust funds, such return will not be a preference, for neither is the claimant a creditor nor the return a transfer.⁷

§ 1307³. Deposits in Bank on Eve of Insolvency, Whether Constitute Trust Fund.—The doctrine seems to be thoroughly established that the receiving of deposits on the eve of insolvency by a bank does not give rise to the relation of debtor and creditor but constitutes a fraud on the part of the bank towards the depositor, the deposit constituting a trust fund reclaimable by the depositor.

In *re Silver*, 31 A. B. R. 106, 208 Fed. 797 (D. C. Ohio): "We hold then that the facts surrounding this transaction justified petitioners' claim that the bankrupt legally knew of the insolvency of his business when he received the deposits in question. The implied contract, therefore, which ordinarily arises to create the relation of debtor and creditor when deposits are made in a banking institution never was created, and a trust impressed upon these funds in behalf of these several depositors is the equitable result of these transactions."

§ 1308. One Benefited Must Hold Provable Claim, Else Not Preference.—A transfer or judgment to constitute a preference must operate to give a "creditor" a greater percentage of his claim than other creditors.⁸ Now, "creditor" is defined by § 1 (9) to include anyone who owns a demand or claim provable in bankruptcy.⁹ Hence it necessarily follows, that where the one benefited does not hold a provable claim, a preference has not been given. And the date of the filing of the bankruptcy petition fixes the status of the creditor's claim.¹⁰

Clarke v. Rogers, 26 A. B. R. 413, 183 Fed. 518 (C. C. A. Mass., affirmed in 228 U. S. 534, 30 A. B. R. 39, quoted at §§ 1307½, 1313 4-10): "* * * it seems to be an accepted doctrine that preferences are within the same subject matter as claims provable, and it is only with reference to claims provable that preferences can be declared. *Richardson v. Shaw*, 209 U. S. 365, * * * while the definition of 'creditor' and 'debt' do not assume to be exclusive but only inclusive, nevertheless it is undoubtedly the general construction of the statutes in bankruptcy that nothing is within their purview so far as preferences are concerned, except with reference to debts which can be proved for a dividend. On the other hand, it must be accepted that anything

7. Compare post, § 1883.

8. Bankr. Act, § 60 (a). As to what are provable claims, see ante, chapter XXI. In *re Crafts-Riordan Shoe Co.*, 26 A. B. R. 449, 185 Fed. 931 (D. C. Mass.), quoted in note to § 1282.

9. *Clarke v. Rogers*, 26 A. B. R. 413, 183 Fed. 518 (C. C. A. Mass.), affirmed in 30 A. B. R. 39, 228 U. S. 534.

10. See ante, §§ 629, 669.

which can be proved for a dividend is within the purview of those portions of the statutes which relate to preferences, whether or not they are strictly shadowed out by the words 'creditor' and 'debt' as especially defined in the statute or as otherwise reasonably understood."

The mere fact that a transferee had brought a suit on contract, no judgment having rendered thereon, probably would not be sufficient proof that the demand was a claim of a creditor, unless the other evidence or the pleadings obviates the necessity of such proof.¹¹

§ 1308¹. Revival of Outlawed Debt.—A bankrupt may revive an outlawed debt if the debt be bona fide, at any time before the filing of the bankruptcy petition, even though his motive be to qualify the creditor for sharing in dividends.

In *re Banks*, 31 A. B. R. 270, 207 Fed. 662 (D. C. N. Y.): "I cannot hold that a payment made immediately before bankruptcy, or filing a petition in bankruptcy, to renew an outlawed debt and to enable the creditor to come in and share in the distribution, the one receiving it having no reasonable cause to believe it will operate as a preference, is a fraud on creditors or the law."

§ 1309. Payment or Other Transfer on Claim for Personal Injury, etc., Not Preference.—Payments or other transfers to persons holding claims for personal injuries are not transfers to "creditors," within the meaning of the Act, and do not constitute preferences.¹²

§ 1310. Payment or Other Transfer Made to or Enuring to Benefit of Surety, Endorser, etc., of Bankrupt, Even before Principal's Default or before Payment by Surety—Preference.—Thus, on the other hand, payments or other transfers to sureties, endorsers, etc., or enuring to their benefit, may be preferences to them even before the bankrupt principal's default and before any payment by the surety or endorser; for sureties, endorsers, etc., are "creditors" from the signing of the obligation and before default by the principal or payment by the surety.¹³

11. In *re Crafts-Riordan Shoe Co.*, 26 A. B. R. 449, 185 Fed. 931 (D. C. Mass.).

12. See ante, chapter XXI, "Claims Ex Delicto," § 635.

13. In *re Stout*, 6 A. B. R. 505, 109 Fed. 794 (D. C. Mo.), quoted, ante, § 644; *Livingston v. Heineman*, 10 A. B. R. 39, 120 Fed. 787 (C. C. A. Ohio, reversing In *re New*, 8 A. B. R. 566), quoted ante, § 644; *Swarts v. Siegel*, 8 A. B. R. 694, 695, 117 Fed. 13 (C. C. A. Mo.), quoted ante, § 644; In *re O'Donnell*, 12 A. B. R. 621, 131 Fed. 150 (D. C. Mass.), quoted ante, § 644; *Swarts v. Fourth Nat'l Bk.*, 8 A. B. R. 673, 117 Fed. 1 (C. C. A. Mo.); In *re Lyon*, 10 A. B. R. 25, 121 Fed. 723

(C. C. A. N. Y., affirming 7 A. B. R. 412); *Crandall v. Coats*, 13 A. B. R. 712, 133 Fed. 965 (D. C. Iowa); *Landry v. Andrews*, 6 A. B. R. 281, 48 Atl. 1036 (Sup. Ct. R. I.); In *re Matthews & Rosenkranz*, 15 A. B. R. 721 (Ref. Mass.); In *re Sanderson*, 17 A. B. R. 871 (D. C. Vt.). That sureties and endorsers are "creditors" from the date of signing, and even before default or payment by themselves, see ante, chapter XXI, "Provable Debts," div. 3. "Contingent Claims," §§ 642, 643. *Kobusch v. Hand*, 19 A. B. R. 379, 156 Fed. 660 (C. C. A. Mo.); In *re Bailey & Son*, 21 A. B. R. 911, 166 Fed. 982 (D. C. Pa.). Compare, In *re Farmers Supply Co.*, 22 A. B. R. 460, 170 Fed. 502 (D. C. Ohio); *Brown*

McAtee v. Shade, 26 A. B. R. 151, 185 Fed. 442 (C. C. A. Mo.): "Mr. Quinn having thus endorsed these notes at once became liable to the bank (the creditor) either as maker or guarantor for their payment, if there was a valid consideration for his endorsement of them, and at the same time became a creditor of the bankrupt."

Lazarus v. Eagan, 30 A. B. R. 287, 206 Fed. 518 (D. C. Pa.): "There is, furthermore, no doubt that at the time of the transfer Greggs was Eagan's creditor by reason of the endorsement of the note at bank. That an indorser or surety on a note may be a creditor within the meaning of the bankruptcy law has been held in a long line of cases. Eagan having permitted or induced payment of the note, thereby intending to relieve himself from payment of all or a portion of it, to that extent was benefited and constituted him a creditor."

Under this doctrine, payment to a holder has been held a preference to an accommodation endorser.¹⁴

§ 1311. Payment or Other Transfer to Present Owner of Claim, Preference to Both Present Owner and Also to Transferrer, if Transferrer Remains Bound as Surety or Endorser.—The payment of the bankrupt's note to the endorsee of the original creditor, or to the present owner, may constitute a preference to the endorsee or original creditor as of the date of the payment, notwithstanding the benefit of the payment may enure also to a surety or endorser.

In *re Geo. M. Hill Co.*, 12 A. B. R. 221, 120 Fed. 315 (C. C. A. Ills.): "It is insisted by the appellant that payment by the bankrupt of notes given by it to third parties and discounted by the bank were, under the law, preferential payments to those for whom the bank discounted the notes, and were not preferential payments to the bank. We are not able to concur in this contention. * * * Within the definitions of the Bankruptcy Act the indorser has been held to be a creditor of the bankrupt, while his liability as endorser is contingent, so as to charge him with preferential payments made to the holder of the note. *Swarts v. Siegel*, 8 A. B. R. 689, 117 Fed. 13. But none the less is the owner of the note likewise subjected to the penalties of the act for receipt of such preferential payment. *Swarts v. Fourth Nat'l Bk. of St. Louis*, 8 A. B. R. 673, 117 Fed. 1. In these cases both the bank and the endorsers were held chargeable for receipt of preferential payment by reason of the amount paid to the bank which payment must be refunded before either party could prove an independent claim against the bankrupt with which the other party was in no wise connected. This would not result, as counsel supposed, that in such case the insolvent estate would recover twice what it lost. Only the amount by which the assets of the estate had been depleted must be returned."

v. Streicher, 24 A. B. R. 267, 177 Fed. 473 (D. C. R. I.).

Bank of Wayne v. Gold, 26 A. B. R. 722, 146 (App. Div. N. Y.) 296, 130 N. Y. Supp. 942; *Stern v. Paper Co.*, 28 A. B. R. 592, 198 Fed. 642 (C. C. A. N. Dak.). Compare inferentially, *Page v. Moore*, 24 A. B. R. 745, 179 Fed. 988 (D. C. Pa.). *United Surety Co. v. Iowa Mfg. Co.*, 24 A. B. R. 726, 179 Fed. 55 (C. C. A. Mo.).

Surety on Government Contract Advancing Money to Meet Payroll and Taking Cognovit Note Therefor and Levying Judgment Same Day.—*United Surety Co. v. Iowa Mfg. Co.*, 24 A. B. R. 726, 179 Fed. 55 (C. C. A. Mo.). But compare post, § 2191.

14. Obiter (reasonable cause of belief not proved). *Reber v. Shulman & Bro.*, 24 A. B. R. 782, 179 Fed. 574 (D. C. Pa.).

On the other hand, the payment of the bankrupt's note to an endorsee of the original creditor likewise may constitute a preference upon the original debt, as of the date of the payment: it enures to the benefit of the endorser or original creditor (if the original creditor is still bound), and gives him a preference.¹⁵

In *re Meyer*, 8 A. B. R. 598, 115 Fed. 997 (D. C. Tex.): "The debt of Walshe & Co. (the original creditor) was reduced by the payments made by the bankrupt to Brooke, Smith & Co. (the endorsee), and therefore Walshe & Co. enjoyed the fruits of such payments as much as if they had been made direct to them. It would be inequitable and unjust to other creditors to say that they had received nothing on the \$350 note given them by the bankrupt."

But in one case it is held to be a preference as of the date of the receipt by the indorser of the consideration from the endorsee.¹⁶

The original transferrer or indorser, or (if still bound) the original creditor, must surrender the preference (if "received with reasonable cause" since the Amendment of 1903) before he can have his claim allowed; for the payment, though made to another, is nevertheless made to extinguish the original claim and the original claimant receives benefit thereby.¹⁷ And the trustee may recover the payment from the endorser, if the payment was made at his request, to relieve him, and with reasonable grounds existing on the indorser's part to believe a preference would be effected thereby.¹⁸

15. In *re Lyon*, 10 A. B. R. 25, 121 Fed. 723 (C. C. A. N. Y., affirming 7 A. B. R. 412); *Landry v. Andrews*, 6 A. B. R. 281, 21 R. I. 597; In *re Matthews & Rosenkranz*, 15 A. B. R. 721 (Ref. Mass.); In *re Waterbury Furniture Co.*, 8 A. B. R. 79, 114 Fed. 255 (D. C. Conn.); (1867) *Bartholomew v. Bean*, 18 Wall. 635; (1867) *Ahl v. Thorner*, 3 N. B. R. 118, Fed. Cases, No. 103.

16. In *re Weissner*, 8 A. B. R. 177 (D. C. N. Y.).

17. In *re Matthews & Rosenkranz*, 15 A. B. R. 721 (Ref. Mass.); In *re Waterbury Furn. Co.*, 8 A. B. R. 79, 114 Fed. 255 (D. C. Conn.); *obiter*, In *re Wyly*, 8 A. B. R. 604 (D. C. Tex.); In *re Meyer*, 8 A. B. R. 598, 115 Fed. 997 (D. C. Tex.).

Contra, see *obiter*, In *re Bullock*, 8 A. B. R. 646, 116 Fed. 667 (D. C. N. Car.): This question was not necessary to be decided, for there was no proof of insolvency at the time of the payments, anyway.

Compare, apparently contra, In *re Weissner*, 8 A. B. R. 177 (D. C. N. Y.), where the court held, that money received from third party by creditor on discounting bankrupt's note constituted a preference as of the date the discount money was applied on the bankrupt's debt, although the bank-

rupt did not pay anything out of his estate until the note matured. This does not seem to be good law, however.

Compare, apparently contra, In *re Harpke*, 8 A. B. R. 535 (C. C. A. Wis.), where the court held, that the holder of the bankrupt's unindorsed note is not debarred from proving his claim thereon, because within the four months period he received from the endorser payment of another note, having reason to believe that the money therefor had come from the bankrupt, though in ignorance of his insolvency at the time of such payment. This would be good law now, since the amendment of 1903 exonerates from the necessity of surrender those receiving preferences without reasonable grounds, etc.; but, *quære*, whether it was good law when enunciated. The classification of unindorsed and indorsed notes into separate classes also is not correct.

18. *Landry v. Andrews*, 6 A. B. R. 281, 21 R. I. 597.

Compare, where facts held insufficient to show that the president of a bankrupt corporation had caused it to make the transfer in order to relieve him from his endorsement. *Page v. Moore*, 24 A. B. R. 745, 179 Fed. 988 (D. C. Pa.).

Kobusch v. Hand, 19 A. B. R. 379, 156 Fed. 660 (C. C. A. Mo.): "Where the surety is the president of the Bankrupt, and with knowledge of its insolvency directs the payment to the holder of the obligation with intent to relieve himself from liability and to secure an advantage over other creditors, a preference arises which may be recovered from him by the trustee."

§ 1312. Partner Selling Out to Remaining Partner, Not Preference to Individual Creditors.—Where a partner sells out to his sole co-partner, the partnership being insolvent, it has been held, that, in effect, a preference has been made by the partnership to the individual creditors.¹⁹ But this would hardly be a case of preference, for the preference, to be such, must be to a creditor of the bankrupt, but such a transfer does not give any advantage to any creditor of the bankrupt partnership. It simply puts the property out of the reach of all partnership creditors until the individual creditors of the remaining partner have been paid.^{19a}

The placing of a custodian in charge of a partnership store by agreement of all parties, to receive the proceeds of sales and to apply the same upon an execution on an individual judgment against one of the partners, the judgment and all the other proceedings occurring within the four months preceding the bankruptcy of both partners and of the partnership, has been held to constitute a preference.²⁰

But here again it was not a preference because the transfer was not to a creditor of the bankrupt. It was simply a diversion of partnership funds to one receiving the funds with knowledge.²¹

§ 1312¹/₄. Transfers of Individual Property Whether Preferences in Partnership Bankruptcies.—In general, transfers by one member of an insolvent partnership of his individual property within four months of the bankruptcy of the partnership are not preferences in the partnership bankruptcy.²²

Obiter, Mills v. Fisher & Co., 20 A. B. R. 237, 159 Fed. 897 (C. C. A. (Tenn.): "But it is not an act of bankruptcy for which a firm may be adjudged a bankrupt, that one of its members, out of his individual estate, prefers one of his own or one of the firm's creditors. * * * The application by one partner of his individual property to the payment of one firm creditor would be an

19. *In re Head & Smith*, 7 A. B. R. 556, 114 Fed. 489 (D. C. Ark.). Compare, post, § 2269.

19a. *In re Denning*, 8 A. B. R. 133, 114 Fed. 219 (D. C. Mass.), quoted at § 2270; however, compare doctrine of § 2268¹/₄.

20. *In re Metzger Toy & Novelty Co.*, 8 A. B. R. 307, 114 Fed. 957 (D. C. Ark.). In this case there was no need of proof of "reasonable grounds for belief" because it arose upon the refusal of the court to allow a claim until preferences had been surrendered and arose before the amendment of

1903 made the existence of such reasonable grounds a necessary element in barring a claim on account of preference.

21. See post, § 2268, et seq.

22. *Miller v. (New Orleans) Acid & Fertilizer Co.*, 21 A. B. R. 416, 211 U. S. 496, affirming 117 La. 821. *Obiter, Mayes v. Palmer*, 31 A. B. R. 225, 208 Fed. 97 (C. C. A. Mo.).

Compare corresponding proposition under "First Element of a Preference," ante, §§ 1290, 1291; also, compare post, § 1387¹/₂.

individual act, and not the joint act of the firm, and, therefore, not an act for which the firm could be adjudged bankrupt."

That is, they are not preferences unless the individual member be also adjudged bankrupt in the same proceedings.^{22a}

But a transfer of individual assets by one member to pay a firm creditor a greater percentage than another firm creditor would get from the same individual estate, may be a preference, since the individual estates constitute, sub modo, funds to which partnership creditors are entitled to resort, in proper order of priority after individual creditors are satisfied in full, so that a transfer to one firm creditor without a like transfer to other firm creditors would be the giving of a greater percentage to one creditor than to another of the "same class" in the order of priority.²³

And such an individual transfer may be a voidable preference in a partnership bankruptcy by state law, of which the trustee may avail himself by subrogation to the rights of any creditor who has already instituted proceedings.²⁴

§ 1312½. Transfers of Partnership Property, Whether Preference in Individual Bankruptcies.—Bankruptcy proceedings against one partner do not affect the validity of a transfer made by the partnership.²⁵

Thus, preferences given by a partnership on partnership property that is being administered in the individual bankruptcy proceedings of one of the partners, are not affected.²⁶

§ 1312¾. Transfers to Creditor's Agents.—Of course, transfers to a creditor's agent or to one acting as a go-between are within the prohibition: *quid facit per alium, facit per se*.²⁷

§ 1313. When Stock Broker's Customer Becomes "Creditor."—The various relations into which stock brokers and their customers get themselves by their different transactions have given rise to considerable discussion. As to a broker buying and selling stock on margin for customers, it has been held in Massachusetts and in some other states that his relation to customers is that of debtor and creditor and not that of fiduciary and beneficiaries, and that a payment upon a running account between them may be a preference.²⁸

In *re Dorr*, 28 A. B. R. 505, 196 Fed. 292 (C. C. A. Cal.): "In the case at bar there was no pledge or contract of pledge. What the bankrupt did for the

^{22a} Compare post, § 2268¼.

²³ Compare post, § 2268¼; also see *Mills v. Fisher & Co.*, 20 A. B. R. 237, 159 Fed. 897 (C. C. A. Tenn.).

²⁴ *Miller v. New Orleans Acid & Fertilizer Co.*, 21 A. B. R. 416, 211 U. S. 496 (affirming 117 La. 821).

²⁵ *McNair v. McIntyre*, 7 A. B. R. 638, 113 Fed. 113 (C. C. A. N. Car.).

²⁶ *McNair v. McIntyre*, 7 A. B. R. 638, 113 Fed. 113 (C. C. A. N. Car.).

²⁷ See ante, "Indirect Preferences," § 1300; also see *Alexander v. Redmond*, 24 A. B. R. 620, 182 Fed. 92 (C. C. A. N. Y.).

²⁸ In *re Gaylord*, 7 A. B. R. 577, 111 Fed. 117 (D. C. Mo.).

For Massachusetts cases, see citations in *Richardson v. Shaw*, 19 A. B. R. 717, 209 U. S. 365.

appellant was to purchase options, or the right to buy grain for future delivery. The appellant paid the bankrupt 3 per cent of the value of the grain which he wished to purchase. He did not aim to purchase grain at that time, but to secure the right to purchase it at a future time. The bankrupt telegraphed the orders to Wrenn & Co., members of the Chicago Board of Trade. They went upon the Exchange in Chicago and entered into a contract with some other member thereof by which the latter agreed to deliver to them at any time in the month named the amount of corn specified in the order. Under the contract no grain was delivered to the bankrupt, and he made no advances thereon and held nothing in pledge. He was accountable to the appellant for balances in his favor, if any there were after selling the grain and making such offsets as were chargeable against the proceeds."

On the other hand, it has been held in New York, and by the United States Supreme Court, and it is the weight of authority, that where a stock broker pledges his customer's stocks in general loans, the customer for whom stocks are carried by the broker is not a creditor and does not receive a voidable preference, although he knows the broker to be insolvent, when he closes the transaction, pays the balance owing the broker and receives stocks worth more in the market than the sum paid to take them up. The customer simply redeems his stock from the broker's lien by "paying up."²⁹

§ 1313 1/10. **Public Corporations as Creditors.**—There seems to be no reason for exempting public corporations, except of course when acting in their governmental capacity, from the ordinary rules pertaining to preferential transfers; and no State law can exempt them therefrom.³⁰ Thus, a preferential transfer to a township may be set aside.³¹

§ 1313 2/10. **One Bankrupt Estate as Preferred Creditor of Another.**—The act in § 57 (m) provides that "the claim of any estate which is being administered in bankruptcy against any like estate may be proved by the trustee and allowed by the court in the same manner and upon like terms as the claims of other creditors."

Where a trustee himself became bankrupt, a preference was charged in the later bankruptcy against the former estate as a creditor.³²

29. *Richardson v. Shaw*, 16 A. B. R. 842, 147 Fed. 59 (D. C. N. Y., affirmed in 16 A. B. R. 876); *Richardson v. Shaw*, 16 A. B. R. 876 (D. C. N. Y., affirming 16 A. B. R. 842); compare, analogously, *In re Bolling*, 17 A. B. R. 399, 147 Fed. 786 (D. C. Va.); also compare, analogously, *In re Berry & Co.*, 17 A. B. R. 468 (C. C. A. N. Y.). See, in addition, *Richardson v. Shaw*, 19 A. B. R. 717, 209 U. S. 365 (affirming 16 A. B. R. 876, also 147 Fed. 59). Also compare, analogously, *In re Berry & Co.*, 17 A. B. R. 468 (C. C. A.

N. Y.), affirmed sub nom. *Thomas v. Taggart*, 19 A. B. R. 710, 209 U. S. 385.

30. Compare situation as it appears from records in *United Surety Co. v. Iowa Mfg. Co.*, 24 A. B. R. 726, 179 Fed. 55 (C. C. A. Mo.). Compare, also, post, § 2191.

31. *Painter v. Napoleon Tp.*, 19 A. B. R. 412, 156 Fed. 289 (D. C. Ohio), quoted at § 1414.

32. *Block, trustee, v. Rice, trustee*, 21 A. B. R. 691, 167 Fed. 693 (D. C. Pa.).

§ 1313 3 10. Delivery to Purchaser Who Has Paid in Advance, Whether Preference.—Where a purchaser from the bankrupt has paid partly in advance, the delivery of the goods purchased has been held not to be a preference, if the transaction be bona fide; for the purchaser is not a “creditor” but is, rather, a debtor for the balance due.³³

Templeton, Trustee, *v.* Kehler, 23 A. B. R. 41, 173 Fed. 574, 575 (D. C. Pa.): “But here there was no antecedent debt, and therefore no preferential payment could be made. The defendant was buying cattle from the bankrupt in the usual course of business, and had advanced money in part payment. The cattle were delivered (the price being concededly fair) and the defendant became the bankrupt’s debtor for the balance of the price. * * * He was not the bankrupt’s creditor in any proper sense, but is rather to be regarded as the bankrupt’s debtor.”

Yet such could not be the rule unless title to the goods had already vested in the purchaser or there were some equitable lien thereon in the purchaser’s favor, since, if it were simply a payment in advance, then the purchaser was a creditor to the amount theretofore paid, the bankrupt fulfilling his obligation by delivery of goods instead of money.

§ 1313 4/10. Transfer by Bankrupt to Himself in Another Capacity.—A bankrupt, by transferring assets to himself in another capacity, may thereby create a preference; thus, where a bankrupt, as guardian, had misappropriated trust funds, transfers from his individual estate to make good the defalcation were held to be preferences in his individual bankruptcy.

Clarke *v.* Rogers, 228 U. S. 534, 30 A. B. R. 39 (affirming 26 A. B. R. 413, 183 Fed. 518): “The question in the case is, Do these facts show a preference within the meaning of the bankruptcy law? Putting to one side the identity of Shaw as an individual and Shaw as the trustee of the trusts, there are the elements of a preference. In other words, there is indebtedness; Shaw is indebted to all of the estates of which he was trustee. He used his individual property to pay the indebtedness of the Parsons trust, and he thus gave that trust a preference over the others. It was enabled to the extent of the property transferred to obtain a greater percentage of its debts than the other trusts. * * *.

“But this, appellant contends, is to evolve ‘two moral persons out of one embezzler.’ The criticism only can be made by putting out of view what the ‘one embezzler represents. He is one being but acts in more than one capacity, and in all of his capacities he has duties and obligations. The relation of a trustee to the trust property is not the same as his relation to his individual property. He certainly may incur obligations to the trust. He can only satisfy the obligations out of his individual property, and by doing so may deplete it, make it deficient, to satisfy its obligations. These are realities not fictions. We must overlook essential things to disregard them. * * *

“To the contention that two persons were necessary to consummate a pref-

³³ Compare, instances of equitable liens for advances on goods in process of manufacture, ante, § 1147, and post, § 1372; also *Gage Lumber Co. v.*

McEldowney, 30 A. B. R. 251, 207 Fed. 255 (C. C. A. Ky.); also compare § 1316.

erence, one to transfer and the other to receive the property, the court answered [the court in the case quoted] answered: 'But where the same person acts as the giver and receiver of the security, the concurrence and participation of two parties to the fraudulent preference exist. * * * One individual acting in two capacities, as debtor and on behalf of the creditor, may constitute the two persons contemplated by the statute.'

"And supplying the element of knowledge of the insolvency and the preference required by the statute, the court said that the ward was bound by the knowledge of his guardian. * * * As we have said, there may be a unity of the person in the individual and the trustee, of the individual and the guardian; we must look beyond it to the difference in his capacities and the duties and obligations resulting from it. These duties and obligations are as distinct and insistent as though exercised by different individuals, and have the same legal consequences."

Clarke *v.* Rogers, 26 A. B. R. 413, 183 Fed. 518 (C. C. A. Mass.), affirmed in 228 U. S. 534, 30 A. B. R. 39. "Neither, as we have said, is there any difficulty arising from the fact that, in these transactions, Shaw as an individual was dealing with himself as trustee. * * * In other words, it follows beyond all question that we cannot find that what occurred here was not a preference in the event we should be compelled to find that the same transactions were a preference when passing between Shaw as an individual and his successor in the trust."

Rogers *v.* American Halibut Co., 31 A. B. R. 576 (C. C. A. Mass.): "The bankrupt was the general business manager of the defendant corporation and within the prescribed period he paid the bookkeeper in partial settlement of overdrafts of his accounts with the company the amount in controversy. His insolvency when he made the payment is conclusively shown by his own evidence * * * besides, his knowledge that he was insolvent is to be imputed to the defendant [corporation] and if believed, the evidence would have justified the jury in finding that as manager, charged with the supervision of its business, he had reasonable cause to believe the company's debt would be largely satisfied to the detriment of his other creditors."

§ 1314. Third Element of a Preference—Creditor's Claim Must Have Been Pre-Existing Debt.—The creditor's claim must have a debt—a pre-existing debt: and the transfer will not amount to a preference if made contemporaneously with (or before) the rising of the claim. Preference implies preceding credit.

Section 60 as before noted must be read in conjunction with § 67 (d), among other sections in *pari materia*. Section 67 (d) is the converse of § 60 so far as transfers by way of lien are concerned, and protects all bona fide liens, duly recorded, where recording is requisite, that are based upon a "present consideration." "Present consideration" in this connection must be given a broader construction than it usually possesses. As the term is commonly used, it is interchangeable with "valuable consideration." Thus, for instance, the extension of time for the payment of a pre-existing debt is commonly held to be a present or "valuable" consideration for a transfer based thereon. And well enough so when the debtor is solvent, for when he is solvent it makes no difference whether his liabilities are reduced or his assets increased—the net result is the same, for the payment of the debt

is equivalent to an increase of his assets by just so much. But when a debtor becomes insolvent it is manifestly quite different—it makes a great difference then whether the transaction results in an increase of the common fund or merely in a reduction of the liabilities.

So it is that by the term "present consideration" as used in this connection in bankruptcy is meant not a reduction of liabilities, but an increase or exchange of assets; and thus a lien given merely to secure a pre-existing debt is not—even though not made nor accepted in contemplation of bankruptcy—a valid lien, but if given for money or property then and at that present time passing into the estate, it is valid, unless, of course, it is affected by bad faith.³⁴

34. *Ernst v. Mechanics', etc., Bank*, 29 A. B. R. 289, 201 Fed. 664 (C. C. A. N. Y.); *Lindley v. Ross*, 29 A. B. R. 610, 200 Fed. 733 (C. C. A. Ill.); instance, *In re Herman*, 31 A. B. R. 243, 207 Fed. 594 (D. C. Iowa); instance, deed to secure preceding indebtedness. *Northern Neck State Bank v. Smith*, 30 A. B. R. 527, 205 Fed. 894. (C. C. A. Va.); *Simmons v. Greer*, 23 A. B. R. 443, 174 Fed. 654 (C. C. A. S. Car.), quoted, on other points, § 1225½; *Lesser v. Bradford Realty Co.*, 15 A. B. R. 123, 47 N. Y. Misc. 463 (N. Y. Sup. Ct.); *In re Wright Lumber Co.*, 8 A. B. R. 345, 114 Fed. 1011 (D. C. Ark.); *In re Clifford*, 14 A. B. R. 283, 136 Fed. 475 (D. C. Iowa); *In re Little River Lumber Co.*, 1 A. B. R. 483, 92 Fed. 585 (D. C. Ark.); *Bank v. Bruce*, 6 A. B. R. 313, 109 Fed. 69 (C. C. A. S. C.); *In re Durham*, 8 A. B. R. 115, 114 Fed. 750 (D. C. Md.); impliedly, *In re Rudnick*, 4 A. B. R. 531, 102 Fed. 750 (D. C. Wis.). See, however, *In re Mandel*, 10 A. B. R. 774, 127 Fed. 863 (Ref. N. Y.); *Morgan v. Nat'l Bk.*, 16 A. B. R. 645, 145 Fed. 466 (C. C. A. W. Va.); *In re Soudans Mfg. Co.*, 8 A. B. R. 45, 113 Fed. 804 (C. C. A. Ind.); *In re Cobb*, 3 A. B. R. 129, 96 Fed. 821 (D. C. N. Car.); obiter, *In re Pease*, 12 A. B. R. 68, 129 Fed. 446 (D. C. Mich.); *In re U. S. Food Co.*, 15 A. B. R. 329 (Ref. Mich.); *Crim v. Woodford*, 14 A. B. R. 302, 136 Fed. 34 (C. C. A. W. Va.); *In re Noel*, 14 A. B. R. 715, 137 Fed. 694 (D. C. Md.); *Young v. Upson*, 8 A. B. R. 377, 115 Fed. 192 (D. C. N. Y.); *Parker v. Black*, 16 A. B. R. 205, 143 Fed. 560 (D. C. N. Y.); *Iron & Supply Co. v. Roll Mill Co.*, 11 A. B. R. 200, 125 Fed. 974 (D. C. Ala.).

Impliedly, *In re First Nat'l Bk. v. Penna. Trust Co.*, 10 A. B. R. 782, 124 Fed. 968 (C. C. A. Penn.). In this case, before the four months period a

bank took a lot of billets as security for two notes. One note was paid within the four months period and thereafter a new loan was made on the strength of the same security. Meanwhile the sign that the steel billets had been pledged was taken down by mistake. On the discovery of the mistake the sign was replaced: held, not to constitute a preference.

Instance, *In re Graff*, 8 A. B. R. 745, 117 Fed. 343 (D. C. N. Y.): Payment on day of assignment of balance due to stock broker's bookkeeper for money left on deposit to buy shares, is a preference that must be surrendered before his claim for stock converted can be allowed.

Instance, *Martin v. Hulen*, 17 A. B. R. 510 (C. C. A. Mo.): Practically contemporaneous transaction. At time of purchasing giving chattel mortgage on goods purchased which covered future additions and then immediately consolidating old stock with goods purchased—held, no preference.

Instance, compare, inferentially, *In re Graff*, 8 A. B. R. 744 (D. C. N. Y.): Stockbroker's customer leaving on deposit money for purchase of stock, stock purchased is not a preference.

Instance, *Sabin v. Camp*, 3 A. B. R. 578, 98 Fed. 974 (D. C. Ore.): Consummation of purchase within four months period.

Instance, *In re Gesas*, 16 A. B. R. 872 (C. C. A. Idaho): Banker's lien held not to cover stocks of merchandise, live stock, etc., but only securities, etc. See post, § 1506.

Compare [surety on government contract advancing money to meet payroll and at same time taking judgment note therefor upon which takes immediate judgment and levies, all in same day, yet held preference], *United Surety Co. v. Iowa Mfg. Co.*, 24 A. B. R. 726, 179 Fed. 55 (C. C. A. Mo.).

Tiffany v. Institution, 18 Wall. 375: "The preference at which this law is directed can only arise in the case of an antecedent debt."

In *re Wood & Henderson*, 20 A. B. R. 1, 210 U. S. 246: "This [payment of attorney in advance for services to be rendered in bankruptcy] is not a case of preference, where part of the estate is transferred to a creditor so as to give him more of the estate than to others of the same class, under § 60. * * * It is a transfer in consideration of future services, to be reduced if found unreasonable in amount."

Davis v. Turner, 9 A. B. R. 716, 120 Fed. 605 (C. C. A. N. Car.): "This would seem to settle the point in question. The previous Bankrupt Act contained, substantially, a provision similar to that in the present law relative to the transfer of property in order to prefer a creditor, but did not make any exception for transactions based upon present consideration; and yet under that act it was held that, where the debtor in good faith makes a transfer for value given at the time, or in pursuance of an agreement made when the consideration passed, such conveyance will not be an act of bankruptcy."

Farmers' Bk. v. Carr, 11 A. B. R. 733, 127 Fed. 690 (C. C. A. S. C.): "The essential principle of the bankrupt law is that all of the bankrupt's property be divided equally, without preference, to the payment of his debts. It abhors preferences. But if bona fide an advance in præsentia be made to one who afterwards within four months becomes a bankrupt, that will be sustained, and a lien therefor held valid."

Stedman v. Bank of Monroe, 9 A. B. R. 4, 117 Fed. 237 (C. C. A. Iowa): "Aside from other provisions of the Bankrupt Act, this recorded chattel mortgage would have been valid security for the prior as well as for the then present loan, according to its terms and purport. It was not illegal, and its continued security of the prior loan merely failed because the bankruptcy of the mortgagor intervened within four months of the giving of the mortgage, and the security, under the terms of the act, became as to the prior loan a preference. But no such result followed in respect to the \$3,000 actually loaned when the mortgage was given."

In *re Davidson*, 5 A. B. R. 528, 109 Fed. 882 (D. C. Iowa): "So the question is, can a bank, knowing a merchant is hard pressed, loan the merchant money with which to pay his debts, the banker at the time, and as part of the same transaction, taking mortgage security, and but for which the money would not have been loaned? * * * The bank did not receive a preference. Without the mortgage, and in the absence of the supposed right to receive the mortgage, the bank would not have parted with its money."

"It is a very different case where one is already a creditor and later insists upon and receives security. Then he may be held to have participated in the preference with all responsibilities. * * *

"The statute certainly cannot be invoked to put an end to legitimate business."

"And if the statute does mean, as is contended by the objecting creditors, then it is readily seen that no business can be transacted with a merchant from the moment he becomes embarrassed."

Furth v. Stahl, 10 A. B. R. 442, 205 Pa. St. 439: "A pledge or payment for a consideration given in the present or to be given in the future, whether in money or goods or services is not a preference. The object of prohibiting preferences is to prevent favoritism whether for secret benefit to himself or other reason among a debtor's creditors, who ought in fairness to stand on the same footing. A transaction by which a debtor parts with something now,

in return for something he acquires or is to acquire in the future, is not within the mischief the act was aimed against."

In *re Busby*, 10 A. B. R. 650, 124 Fed. 469 (D. C. Penn.): "At the time a debt is created, the creditor has the right to dictate the terms on which he will part with his money or property and may, therefore, demand that he shall first be secured to such an extent as satisfies him. With this the Bankruptcy Law does not undertake to interfere, the creditor being allowed to retain without question whatever advantage he has acquired thereby. Bankrupt Act, § 57 e-h. But when a debt is once contracted, payment on account or the transfer of property for the purpose of better securing it, constitutes a preference if the debtor is insolvent at the time, and the result will be to enable the creditor to obtain a greater percentage of his claim than others of the same class. Section 60a. This, in case of the subsequent bankruptcy of the debtor, the law does not allow to go unchallenged. The creditor so preferred must surrender the preference if he desires to participate in the rest of the bankrupt's estate. Section 57g."

In *re Belding*, 8 A. B. R. 719 (D. C. Mass.): In this case a bank appropriated, under a "banker's lien," surplus collateral held for one loan upon another loan, the court saying, "In so far as this lien was given to secure a pre-existing debt, and was without present consideration it would be invalid as a preference."

In *re Great Western Mfg. Co.*, 18 A. B. R. 261, 152 Fed. 123 (C. C. A. Neb.): "The agreement of conditional sale whereby the vendor retained the title to the machinery and material until its purchase price was paid did not create a preference voidable under the bankruptcy law because it was given for a present consideration, for the machinery and material which were and continued to be the property of the vendor, and because it was made more than four months before the petition in bankruptcy was filed."

In *re Union Feather & Wood Mfg. Co.*, 7 A. B. R. 472 (C. C. A. Ills.): "Nor do we think the payments to Goldman were preferences, within the meaning of the Bankruptcy Law. The company in the autumn of 1900, not being insolvent, was in need of ready money to pay its workmen their weekly wages. Goldman came to the assistance of the company, advancing to Peterson the necessary money to meet the pay roll on Saturday night, taking checks for the amounts advanced, which he presented when the company was in funds, and which were then paid to him by the bank. This course of business continued at intervals for some little time. It was rendered necessary by the circumstances, to keep the company a going concern. They were present advances of money upon the checks of the company."

In *re Wolf*, 3 A. B. R. 555, 98 Fed. 84 (D. C. Iowa): "As the security was given for a debt then created, it was a present security, and not a preference which was created by the mortgage."

In *re Porterfield*, 15 A. B. R. 18 (D. C. Va.): "Both the State and Bankrupt Act recognize the right to make a transfer giving preference for a new and not an existing consideration or debt, if made in good faith."

McDonald v. Clearwater R. Co., 21 A. B. R. 182, 164 Fed. 1007 (U. S. C. Idaho): "It is further conceded that a preference is not voidable unless it is given in satisfaction of an antecedent debt—that is, a debt which existed at the time the transfer was made."

The term "antecedent debt" is sometimes used instead of "pre-existing debt." In bankruptcy law, with regard to preferences, antecedent or pre-

existing debt refers to the time of the transfer of the property by which the debt is secured or satisfied in whole or in part.³⁵

In *re Fletcher*, 136 Mass. 242: "The words, 'pre-existing debt,' in their natural meaning include all debts previously contracted, whether they have become payable or not."

§ 1315. Cash Transactions, Not Preferences.—Cash transactions are not within the prohibition.

But if the transactions are really on credit, the mere calling them by usage of trade "cash" transactions will not take them out of the statute.

In *re John Morrow & Co.*, 13 A. B. R. 392, 134 Fed. 686 (D. C. Ohio): "A sale of goods to be paid for in 10 or 30 days is not, in fact, a cash transaction, and cannot, by agreement of the parties, or a usage of merchants, be regarded as such within the meaning of the Bankrupt Law."

§ 1316. Bona Fide Sales, Whether for Cash or on Credit, Not Preferences.—For the same reason, bona fide sales made by the bankrupt up to the very date of the filing of the bankruptcy petition are valid. To be sure the property sold is taken out of the trust fund, but the price, or the promise to pay the price, has taken its place; and the assets—the trust fund—are not depleted.³⁶

^{35.} See also, *Mills v. Virginia*, etc., Co., 20 A. B. R. 750; *Templeton v. Kehler*, 23 A. B. R. 41, 173 Fed. 574, 575 (D. C. Pa.), wherein the terms "antecedent" and "pre-existing" are used interchangeably. Compare, *In re Marstiburn v. Dannenberg*, 117 Ga. 567. Compare, *McDonald v. Clearwater R. Co.*, 21 A. B. R. 182, 164 Fed. 1007 (U. S. C. C. Idaho), quoted *supra*.

^{36.} Instance, purchaser of cotton who has paid in advance for it upon pledged bills of lading attaching the goods on arrival, and making settlement with trustee. *Boden & Haac v. Lovell*, 30 A. B. R. 353, 203 Fed. 234 (C. C. A. Ala.). Compare *Lovell v. Newman*, 27 A. B. R. 746, 192 Fed. 753 (C. C. A.); *Hentz v. Lovell*, 27 A. B. R. 258, 192 Fed. 762 (C. C. A.). Impliedly, *Ohio Valley Bank Co. v. Mack*, 20 A. B. R. 40, 163 Fed. 155 (C. C. A. Ohio). Also impliedly, *contra*, *Sargent v. Blake*, 20 A. B. R. 115, 160 Fed. 57 (C. C. A. Mo.).

Partner Selling Out to Co-Partner When Firm Insolvent.—Where a partnership is insolvent and one of the partners sells out to the other, so that the latter may claim exemptions that could not be claimed as long as the property remained partnership property, the transaction has been held to constitute a transfer to him,

delay and defraud creditors and to be voidable as against the partnership creditors. See *In re Rosenbaum*, 1 N. B. N. 541. Also, see *In re Bergman*, 2 N. B. N. & R. 806; *contra*, see *In re Rudnick*, 102 Fed. 750, 4 A. B. R. 531 (reversing *In re Rudnick*, 2 N. B. N. & R. 769).

Compare, as to right to change non-exempt property into exempt property, *Huenergardt v. Brittain Dry Goods Co.*, 8 A. B. R. 341, 116 Fed. 31 (C. C. A. Kas.); compare, note to *In re Rennie*, 2 A. B. R. 182 (D. C. I. T.).

As to what constitutes bona fides, see *In re Moody*, 14 A. B. R. 276, 134 Fed. 628 (D. C. Iowa).

Bona fide sale of claim against insolvent debtor to one who afterwards buys debtor's business and applies claim on the price, *Hackney v. Hargreaves Bros. Co.*, 13 A. B. R. 164, 68 Neb. 624 (reversing 10 A. B. R. 213).

Partner selling out to third party and taking collateral for the purchase price, *In re Little*, 6 A. B. R. 681, 110 Fed. 621 (D. C. Iowa).

Partner selling out to copartner and then going into bankruptcy, using purchase money to pay creditors, *In re Kindt*, 4 A. B. R. 148 (D. C. Iowa).

Partner Selling Out to Co-Partner When Firm Insolvent.—For this entire subject, see post, § 2268, et seq.

Thus, where there exists a bona fide contract of purchase of the entire output of the bankrupt's lumber mill, the delivery of lumber thereunder, within the four months period, and when the seller was known to be insolvent, has been held not to be a preference, though part of the purchase price had already been advanced.

Mills v. Virginia Carolina Lumber Co., 20 A. B. R. 750, 164 Fed. 168 (C. C. A. N. Car.): "There was no suggestion that the contract made between the Lumber Company and Franklin for the purchase of the entire output of Franklin's mill was not a fair one and one that the law would enforce. The contract was still existing at the time of the adjudication and whatever lumber was on hand as the produce of the mill the Lumber Company had a right to claim, provided it complied with the terms which had been agreed upon. If there had been no payment upon the contract of purchase in advance, the Lumber Company would have been entitled to require the trustee to surrender to it the lumber produced at the mill, provided it complied with the terms of purchase. Having advanced money upon the contract of purchase, the lumber Company thereby became entitled to at least as much of the product of the mill as it had paid for and it could have recovered so much from the trustee, even after the bankruptcy. It is our opinion that at most the taking of the thousand dollars worth of lumber under a claim by the Lumber Company that it was entitled to that specific property by virtue of the contract of purchase cannot be construed into a payment upon an existing debt such as to constitute a preference under the bankruptcy law."

Again, where a purchaser from the bankrupt has paid part of the purchase price in advance, the delivery of the goods to a corresponding amount within the four months period will not constitute a preference; for the delivery is not pro tanto a "transfer" upon a pre-existing debt, the purchaser being a debtor rather than a creditor all the time.³⁷

But it would seem that it must always appear that title to the goods purchased has already passed or that an equitable lien exists or that the money paid in advance is to be kept intact as a distinct fund to become the bankrupt's only on delivery of the goods purchased, otherwise the purchaser is really a creditor.

§ 1317. Payment of Current Rent, Not Preference.—Payment of current rent as it accrues is not a preference; it is upon a contemporaneously arising consideration, rent from its peculiar nature arising out of the property itself, and, constructively at least, being merely a part of the profits from the land, though commuted in money.³⁸

Compare, inferentially, *In re Arnstein*, 2 N. B. N. & R. 106 (Ref. N. Y., affirmed by D. C.): "A contract of lease is peculiar in its nature and differs in many respects from other contracts. Rent as such is an incident to and grows out of the use and occupancy and is the consideration therefor. Unaccrued rent cannot be said therefore to be a fixed liability then absolutely owing, payable in

37. *Templeton*, trustee, *v. Kehler*, 23 A. B. R. 41, 173 Fed. 574, 575 (D. C. Pa.). Compare, ante, § 1313 3-10.

38. Compare, obiter, *In re Lange*, 3 A. B. R. 231, 97 Fed. 197 (D. C. N. Y.).

the future, or indeed a debt of any kind as that word seems to be used in the Act. It is only an unmatured obligation to pay in the future a consideration for future enjoyment and occupancy. This cannot be said to be, properly speaking, a present debt, demand or claim at all, as these words are apparently used in the foregoing provisions, due regard being had to the context, and cannot come within either the clause as to fixed liability then owing, or a debt founded on contract."

But where used as a device for effecting a preference, the payment of current rent may constitute a preference.

In *re Lange*, 3 A. B. R. 231, 97 Fed. 197 (D. C. N. Y.): "Payment of rent by an insolvent is not necessarily a preference. But when it is done as a means and for the purpose of carrying on a business in fraud of creditors it should be so regarded."

And payment of past due rent may constitute a preference unless such rent were a lien on the leasehold, in which event the doctrine of releasing securities of equal value would apply.³⁹

§ 1318. Payment of Interest in Advance Not Preference.—Payment of interest in advance is not a preference.⁴⁰

§ 1319. Present Transfers to Secure Future Advances, Not Preferences.—Likewise, present liens given or transfers made by the bankrupt to secure future advances are not preferences—but are valid to the extent, at least, of the advances actually made.⁴¹

§ 1319¹/₂. Payment of Attorney in Advance Not Preference.—Payment of an attorney for services to be rendered in bankruptcy is not a preference.⁴²

Nor is the securing of the attorney's fees and costs of going into bankruptcy, by way of mortgage or otherwise, a preference; the consideration is a presently passing one, and both items would be entitled to priority of payment out of the estate, in any event.⁴³

§ 1320. Mere Exchanges of Property or Security, Not Preferences.—A mere exchange of one kind of property or security for another of equal value does not constitute a preference.⁴⁴

In *re Manning*, 10 A. B. R. 503, 123 Fed. 180 (D. C. S. C.): "There is nothing in the Bankrupt Law which forbids an exchange of securities, and if a person,

39. See post, § 1325. Also, see *In re Pearson*, 2 A. B. R. 482, 95 Fed. 425 (D. C. N. Y.). In *re Barrett*, 6 A. B. R. 199 (Ref. N. Y.): This case, *In re Barrett*, seems to be based on erroneous reasoning although the conclusion was right in its result. Landlords do not constitute a different "class" within the meaning of § 60 (a). See post, § 1387. Nor is it true that the closing of transactions obviates a preference. See post, § 1421.

40. In *re Keller*, 6 A. B. R. 621, 110 Fed. 348 (D. C. Iowa).

41. *Furth v. Stahl*, 10 A. B. R. 442,

205 Pa. 439; In *re U. S. Food Co.*, 15 A. B. R. 329 (Ref. Mich.).

Compare, as to such mortgage not being void as a transfer hindering, delaying and defrauding creditors, *In re Durham*, 8 A. B. R. 115, 114 Fed. 750 (D. C. Md.). See ante, § 1223.

42. In *re Wood & Henderson*, 20 A. B. R. 1, 210 U. S. 246, quoted at § 2094.

43. In *re Blanchard*, 20 A. B. R. 417, 161 Fed. 793 (D. C. N. Car.). Also, see post, § 1504.

44. See ante, "First Element of Preference," § 1295. *Sawyer v. Turpin*, 91 U. S. 114, quoted ante, under

even while insolvent, makes such exchange as will not diminish the value of his estate, it is unimpeachable; but the court is bound, when such a transaction is reviewed, to satisfy itself that the securities exchanged are of undoubtedly equal value."

Obiter, Iron & Supply Co. v. Rolling Mill Co., 11 A. B. R. 202, 125 Fed. 974 (D. C. Ala.): "An exchange of securities within four months of the proceedings in bankruptcy is not a preference, within the meaning of the Bankrupt Act, if the security given up is a valid one when the exchange is made and if it be of equal value with the security substituted for it, or of not greater value."

In *re Noel*, 14 A. B. R. 715, 137 Fed. 694 (D. C. Md.): "As to the question of preference under the Bankrupt Act, it is clear that a present loan on security is not a preference. * * * This loan was originally made on the security of the mortgage, and there never was a time in all the transactions when Noel had the money without the bank having in hand the mortgage as security. The loan, from its inception, was always secured by the execution of the mortgage, and was always intended to be. If a loan is made upon security, it is not forbidden in good faith to substitute a new security, for the old one."

Deland v. Miller, 11 A. B. R. 744, 119 Iowa 368: "Moreover, it is shown that the mortgage in question was a renewal of another instrument of like character which had been executed by Peterson to the defendants on November 8, 1889. The exchange of these securities did not constitute a preference under the bankrupt law."

McDonald v. Clearwater R. Co., 21 A. B. R. 182, 164 Fed. 1007 (U. S. C. C. Idaho): "Transfers which do not diminish the estate of the bankrupt, but which constitute only a fair exchange of property, are not preferences."

§ 1321. But if New Securities Exceed Value of Old, Preference Arises.—If new securities of greater value are given or additional securities are given, the rule that an exchange of securities is not a preference does not apply;⁴⁵ or if the prior securities were of doubtful value, to the

"First Element of Preference," § 1085; In *re Little River Lumber Co.*, 1 A. B. R. 482, 92 Fed. 585 (D. C. Ark.), and notes. This case was affirmed in 4 A. B. R. 313. *Bank v. Rome Iron Co.*, 4 A. B. R. 441, 102 Fed. 755 (U. S. C. C. Ga.); In *re Cutting*, 16 A. B. R. 753, 145 Fed. 388 (D. C. N. Y.); In *re Shepherd*, 6 A. B. R. 725 (D. C. Ills); In *re Crafts-Riordan Shoe Co.*, 26 A. B. R. 449, 185 Fed. 931 (D. C. Mass.); [1867] *Stewart v. Hopkins*, 30 Ohio St. 531, quoted at § 1325.

Instance, exchange, as per contract, at the rate of 8 old patterns for 7 new ones, not a preference, In *re Nicholas*, 10 A. B. R. 291, 122 Fed. 299 (D. C. N. Y.).

Instance, renewal of insurance policies held as pledges, In *re Little River Lumber Co.*, 1 A. B. R. 482, 92 Fed. 585 (D. C. Ark., affirmed in 4 A. B. R. 313).

Instance, renewal of notes and of pledges of collateral, *Bank v. Rome Iron Co.*, 4 A. B. R. 441, 102 Fed. 755 (U. S. C. C. Ga.).

Instance held not to be such exchange: *Iron & Supply Co. v. Rolling Mill Co.*, 11 A. B. R. 200, 125 Fed. 974 (D. C. Ala.): In this case material was pledged, before the four months period, with a bank for money loaned. In pursuance of an agreement made at the time, portions of the material were permitted to be sold from time to time as needed in the manufacture. Not simultaneously, but later, and within the four months period a lot of accounts were pledged to take the place of the material. The court held that this was not a mere exchange of securities, but was a preferential transfer within the four months period, for the effect of the use of the material was to withdraw it from the pledge weeks before the new security was given.

⁴⁵ In *re Manning*, 10 A. B. R. 500, 123 Fed. 180 (D. C. S. C.); In *re Busby*, 10 A. B. R. 650, 124 Fed. 469 (D. C. Penn.); compare, *Ernst v. Mechanics'*, etc., Nat. Bank, 29 A. B.

extent of the increase of value the transfer may be preferential.⁴⁶

And if the prior mortgage, in exchange for which the one in question was given, was not recorded and is therefore void the transfer has been held to be preferential.⁴⁷

§ 1322. If Securities Remain Same but Indebtedness Secured Increased by Antecedent Debts, Preference as to Antecedent Indebtedness.—And if the securities remain the same, but the indebtedness secured thereby is increased by the addition of antecedent indebtedness, to the extent that such antecedent indebtedness is secured thereby, a preference may exist.

§ 1323. If Securities and Debt Both Increased but Increase of Debt Be for Present Consideration No Preference Arises.—If additional securities are given and the debt also increased, there will be no preference if the increase of the debt was based on a corresponding presently passing consideration.⁴⁸

§ 1324. Withdrawal of Old Security and Substitution of New Must Be Contemporaneous.—The two transactions—the withdrawal of the old security and the substitution of the new—must be contemporaneous; at any rate, the withdrawal must not take place before the delivery of the substituted security.⁴⁹

§ 1325. Payment of Secured Debt, Thereby Releasing Securities.—Payment of a secured debt, at any rate where the securities released thereby go to swell the general estate of the debtor and the benefit from the payment does not accrue solely to other lienholders upon the property, would not be a preference.⁵⁰

R. 289, 201 Fed. 664 (C. C. A. N. Y.); (1867) *Waring v. Buchman*, 19 N. B. Reg. 502.

46. In re Manning, 10 A. B. R. 500, 123 Fed. 180 (D. C. S. C.). Compare, *Ernst v. Mechanics*, etc., Nat. Bank, 29 A. B. R. 289, 201 Fed. 664 (C. C. A. N. Y.).

47. *Brooks v. Bank of Beaver City*, 25 A. B. R. 890 (Sup. Ct. Kan.); *Bank v. Bruce*, 6 A. B. R. 311, 109 Fed. 69 (C. C. A. S. C.).

Contra, *Deland v. Miller*, 11 A. B. R. 744, 119 Iowa 368: "That the prior mortgage was not recorded is immaterial, save on the question as to whether the present one was executed for a present or past consideration."

48. In re Cutting, 16 A. B. R. 754, 145 Fed. 388 (D. C. N. Y.).

49. Inferentially, In re Stedman v. Bank of Monroe, 9 A. B. R. 4, 117 Fed. 237 (C. C. A. Iowa); inferen-

tially, In re Manning, 10 A. B. R. 500, 123 Fed. 180 (D. C. S. C.); compare, *Iron & Supply Co. v. Rolling Mill Co.*, 11 A. B. R. 200, 125 Fed. 974 (D. C. Ala.). To same effect, inferentially, *Bank v. Rome Iron Co.*, 4 A. B. R. 441, 102 Fed. 755 (U. S. C. C. Ga.).

Instance, increasing the security with additional security during the four months will constitute a preference as to the additional security, In re Busby, 10 A. B. R. 650, 124 Fed. 469 (D. C. Penn.).

Instance, replacing depreciated collateral with collateral of no more value than the depreciated collateral originally had is nevertheless a preference to the extent of the depreciation, impliedly, *Iron & Supply Co. v. Rolling Mill Co.*, 11 A. B. R. 200, 125 Fed. 974 (D. C. Ala.).

50. Instance, In re Elm Brew. Co., 12 A. B. R. 623, 132 Fed. 299 (D. C.

[1876] *Stewart v. Hopkins*, 30 Ohio St. 531: "But the payment of a mortgage debt, where the mortgage, as in this case, is full security for the debt, is not a preference within the meaning of the Bankrupt Act. For (as Lord Denman reasoned in *Marshall v. Lamb*, 5 Ad. & Ell. N. S. 115) the assignees have the mortgaged property, and it is indifferent to them whether they have the property free from the mortgage (supposing it to exceed in value the amount of the mortgage) or the property subject to the mortgage and the amount of the mortgage money in cash! It does not diminish the bankrupt's estate available for the payment of his other debts. The payment merely releases the mortgaged premises of the same amount which would otherwise have to be made out of the land for the same purpose by the assignee. It has been repeatedly held by the Supreme Court of the United States that an exchange of property or securities which do not diminish the bankrupt's estate, is not a preference under the Bankrupt Act."

Obiter and merely inferentially, *Page v. Rogers*, 21 A. B. R. 496, 211 U. S. 575: "The defendant therefore contended that, so far as the payments from the purchase money of the coal lands were applied to the indebtedness secured by the trust deed, they were payments for the extinguishment of a valid, subsisting lien upon the land, fixed upon it more than four months before bankruptcy, and therefore not a preference. It may be assumed, without decision, that the payment within four months of a bankruptcy of a mortgage older than four months, and valid inter partes, though unrecorded, cannot be a preference. There is no such case here."

Of course, if the benefit accrues solely to the other lienholders, it might be held to be pro tanto a preference.⁵¹

§ 1325¹/₂. Security Surrendered, However, Must Be on Bankrupt's Property, Else Preference.—The security surrendered, by way of exchange or payment, must have been, of course, on the bankrupt's property, and the surrender of the property of a third person will not constitute the "fair exchange" protected by bankruptcy law.⁵²

§ 1325³/₄. Mechanics' Liens, Landlords' Liens, etc.—As we have

N. Y.): Collecting collateral after bankruptcy of pledgor.

Instance, *In re Riddles' Sons*, 10 A. B. R. 204, 122 Fed. 559 (D. C. Penn.): Payment of interest on mother's dower estate in lands descended to bankrupt from father.

Instance, *In re Pearson*, 2 A. B. R. 482, 95 Fed. 425 (D. C. N. Y.): Payment of back rent which was a lien on a leasehold, thus increasing value of leasehold.

Inferentially, *Wright v. Bank*, 18 A. B. R. 363, 118 N. Y. App. 281. But compare, peculiar instance: payment to creditor having inchoate statutory lien for the purchase price of mine material, notwithstanding acceptance of chattel mortgage, the lien itself not being waived, obiter, *In re Lynn Camp Coal Co.*, 22 A. B. R. 60, 168 Fed. 998 (D. C. Ky.).

Compare, on principle, *Trust & Savings Bank Co. v. Trust Co.*, 229 U. S. 435, 30 A. B. R. 624.

51. Suggestively and inferentially, *In re Elm Brew. Co.*, 12 A. B. R. 625, 132 Fed. 299 (D. C. N. Y.): "The company's property, hence the bank's property, in the certificate, diminished with payment by Vienot. If Vienot paid her whole debt, the company's and bank's interest in the certificate ceased at once and Vienot could compel its surrender to her. Each dollar that the company collected from Vienot correspondingly shrunk the bank's property interest in the certificate."

52. Compare, ante, § 1278. Compare, on the facts, though the case did not turn upon this point, *In re Evans Lumber Co.*, 23 A. B. R. 881, 176 Fed. 643 (D. C. Ga.).

seen, ante, § 1155, mechanics' liens are not preferences, for they are not transfers to pay pre-existing indebtedness but arise, nail by nail, stone by stone, as the building itself rises.

§ 1326. Liens or Other Transfers, Partly on Present Consideration, Partly on Past, Not Wholly Void but Valid Pro Tanto.—Liens given or other transfers made in part for present contributions to the debtor's assets or in exchange for securities of at least equal value, and in part for past contributions or for securities of less value, are not wholly void, but are good pro tanto, that is to say, are good to the extent of the present contributions or the value of the old securities released.⁵³

Bank v. Bruce, 6 A. B. R. 312, 109 Fed. 71 (C. C. A. S. C.): "To the extent, therefore, of the consideration paid at the time of the execution of the note and mortgage, there can be no doubt of the correctness of the decision of the lower court, and it would seem equally clear therefrom that the decision was correct as to the portion of the claim rejected, unless the mortgage of the 7th of October, also securing that portion, constituted a valid lien which entitled appellant, by reason of one security being a mere exchange for the other, to be paid that part of the claim."

Stedman v. Bank of Monroe, 9 A. B. R. 4, 117 Fed. 237 (C. C. A. Iowa): "Aside from other provisions [than 67 (d)] of the Bankrupt Act, this recorded chattel mortgage would have been a valid security for the prior as well as of the then present loan, according to its terms and purport. It was not illegal, and its continued security of the prior loan merely failed because the bankruptcy of the mortgagor intervened within four months of the giving of the mortgage, and the security, under the terms of the act, became as to the prior loan a preference. But no such result followed in respect to the \$3,000 actually loaned when the mortgage was given."

And the same rule applies where part of the consideration is otherwise improper, as for instance, for usury: as to the usury, the lien is void.⁵⁴

Amendment of 1910.—Some decisions having apparently held that § 67d, protecting liens given on presently passing consideration, would pro-

⁵³ In *re Mandel*, 10 A. B. R. 774, 127 Fed. 863 (Ref. N. Y.); In *re Porterfield*, 15 A. B. R. 19, 138 Fed. 192 (D. C. W. Va.); In *re Cobb*, 3 A. B. R. 129, 96 Fed. 821 (D. C. N. Car.); In *re Wolf*, 3 A. B. R. 555, 98 Fed. 84 (D. C. Iowa); In *re Dismal Swamp Contracting Co.*, 14 A. B. R. 175, 135 Fed. 415 (D. C. Va.); obiter, impliedly, In *re Clifford*, 14 A. B. R. 281, 136 Fed. 475 (D. C. Iowa); obiter, *Crim v. Woodford*, 14 A. B. R. 311, 136 Fed. 34 (C. C. A. W. Va.); In *re Hull*, 8 A. B. R. 302, 115 Fed. 858 (D. C. Vt.); inferentially, *Farmers' Bk. v. Carr*, 11 A. B. R. 733, 127 Fed. 690 (C. C. A. S. C.); inferentially, In *re Ronk*, 7 A. B. R. 31, 111 Fed. 154 (D. C. Ind.); In *re Hersey*, 22 A. B. R. 863, 171 Fed. 1001 (D. C. Iowa). In-

stance, In *re White*, 22 A. B. R. 200 (Ref. R. I.).

Compare, In *re Wright Lumber Co.*, 8 A. B. R. 345, 114 Fed. 1011 (D. C. Ark.), where a mortgage given in part for a pre-existing debt and in part for a present loan was held voidable in toto. See post, § 1506.

Compare, In *re Bartlett*, 22 A. B. R. 891, 172 Fed. 679 (D. C. Pa.), where a bill of sale was given within the four months period partly for money paid at the time and partly for pre-existing indebtedness, but where the creditor had not "reasonable ground for believing a preference," so that the transfer was upheld in toto.

⁵⁴ In *re Sawyer*, 12 A. B. R. 269, 130 Fed. 384 (D. C. Mass.).

teet the lien as a whole where given partly upon presently passing consideration and partly for a pre-existing debt, the Amendment of 1910 was passed to set the question at rest and to make positive the rule that such protection would not extend any further than to the presently passing consideration.^{54a}

§ 1326¼. Agreements for Liens or Other Transfers Where Lien Not Given until Later.—It is the date of the actual transfer that governs; and the fact that the transfer was in fulfillment of an agreement which itself was based on a valuable consideration passing between the parties previously will not cause the transfer to relate back to the time of the passing of the original consideration to make it a transfer on a presently passing consideration. It is a transfer on a pre-existing obligation; and may, if the other elements coexist, constitute a preference.⁵⁵

§ 1326½. Ratification within Four Months, of Prior Ineffectual Transfer.—Likewise, a ratification, within the four months period, of an unauthorized or ineffectual transfer made before, it would seem would, on the same principle, take effect as of the date of the effectual transfer; and if then the consideration had already passed, the transfer would be upon a pre-existing indebtedness.⁵⁶

§ 1326¾. Perfecting of Pre-Existing Liens or Rights.—The mere perfecting within the four months period, of liens or rights in the property existing before, does not constitute a preference.⁵⁷

§ 1327. Protection of Liens Given on Presently Passing Consideration, etc.—Liens given on a presently passing consideration, in good faith and not in contemplation of or in fraud upon the bankruptcy act and duly recorded where recording is necessary are protected.⁵⁸

§ 1327½. Amendment of 1910, Whether Debt "Pre-Existing" Determined by Date of Transfer or Recording.—It is the author's view that the question whether the debt, in the paying or securing whereof the transfer is made, is to be deemed a pre-existing debt, is to be determined as of the date of the transfer itself or, if effected by an instrument requiring recording by State statute, then it may be determined as of the date of such recording.⁵⁹

54a. Bankruptcy Act, § 67d, as amended in 1910: "Liens given or accepted in good faith and not in contemplation of or in fraud upon this act, and for a present consideration, which have been recorded according to law, if record thereof was necessary in order to impart notice, shall, to the extent of such present consideration only, not be affected by this act." Also, see post, §§ 1500, 1501.

55. See discussion, post, §§ 1370, 1506. But compare, *McDonald v.*

Clearwater R. Co., 21 A. B. R. 182, 164 Fed. 1007 (C. C. A. Idaho).

56. Compare, facts and holding somewhat to this effect, *In re Mills Co.*, 20 A. B. R. 501, 162 Fed. 42 (D. C. N. Car.).

57. *Sexton v. Kessler*, 21 A. B. R. 807, 172 Fed. 535 (C. C. A. N. Y.); also, see post, §§ 1370, 1372.

58. For a discussion of this subject, see post, division 4 of this chapter.

59. Bankr. Act, § 60 (b), as amended 1910. See post, § 1334½.

It has been held that notwithstanding the Amendment of 1910 to § 60 (b) the debt must have been pre-existing at the time of the original transfer between the parties, else there would be no preference, the amendment merely operating to move on to the date of recording the proof of insolvency and reasonable cause of belief. Whilst this is a possible construction of the amendment, it clearly was not the construction intended by Congress, since the object of the Amendment was to prevent secret liens by causing the whole transaction to be judged as if the transfer took place at the date of the recording, so that if at the date of the recording the consideration did not contemporaneously pass, then it would be a pre-existing indebtedness such as is essential to a preference.

§ 1328. Fourth Element of a Preference.—The debtor must have made a “transfer” of property or have “procured” or “suffered” the creditor to obtain a judgment operating to appropriate property of the debtor. Preference implies voluntary action on the debtor’s part, and a change of title thereby, of the kind known as “transfer” or a seizure by legal proceedings with the debtor’s assent or acquiescence.⁶¹

Tumlin v. Bryan, 21 A. B. R. 319, 165 Fed. 166 (C. C. A. Ga.): “He must prove that the bankrupts * * * (3) made a transfer of their property, i. e., a payment of money.”

In *re Hines*, 16 A. B. R. 500, 144 Fed. 543 (D. C. Pa.): “It is essential to a preference * * * that there should be a transfer by the bankrupt of certain of his property to the creditor preferred.”

Irish v. Citizens’ Trust Co., 21 A. B. R. 39 (D. C. N. Y.): “If the furniture company [the bankrupts] in due course of business had deposited this money with the trust company, and it or any part of it had remained there, the simple relation of debtor and creditor would have arisen, and, in the absence of fraud or collusion or intent to give and receive a preference, there would have been mutual demands which could have been set off, the one against the other, even though the deposits were made within the four months preceding the filing of the petition. * * * But such is not this case. The furniture company checked out the money, all of it so far as involved here, and by checks on the account transferred it to the trust company as a payment of notes with intent to prefer and it was accepted as payment of such notes.”

Inferentially, *Coder v. Arts*, 18 A. B. R. 513, 152 Fed. 943 (C. C. A. Iowa): “The transfer specified in Bankruptcy Act 1898, § 60 (a), includes a mortgage or a lien voluntarily created by the debtor.”

Similarly, where an instrument is left in escrow or where there is a mere written agreement to make a transfer not acted upon at all before bankruptcy, the fact of the obligation itself and that it arose before the four months period will not excuse a payment made upon the strength of the obligation nor bring the payment within the category of transfers not preferential because of their releasing a corresponding value of property from a lien.⁶²

⁶¹ In *re Starkweather & Albert*, 30 A. B. R. 743, 206 Fed. 797 (D. C. Mo.).

⁶² Page *v. Rogers*, 21 A. B. R. 496, 211 U. S. 575, quoted at § 1370.

§ 1329. Voluntary Action of Debtor Requisite to Preference by Way of "Transfer."—Although intent to prefer is not requisite to constitute a transfer a preference, yet there must be at least some voluntary action on the debtor's part or some assent or acquiescence, to constitute the transaction a "transfer." Seizure or appropriation of property by the creditor, or his receipt of it otherwise than by the voluntary act or assent of the debtor, will deprive the transaction of its character as a preference.

Thus, where the property was obtained from the bankrupt by a creditor through fraud or force a preference has not been perpetrated and a suit in replevin or for conversion is the proper remedy.⁶³

Likewise, where it is stolen or embezzled and turned over to the creditor.⁶⁴

Likewise, authority given to a factory by a storekeeper to deduct from each laborer's wages each week the amount then owing to the storekeeper and to remit the same to the storekeeper, gives no authority to the factory to appropriate such deductions on a prior debt owed the factory by the storekeeper, and therefore such appropriation, lacking the element of the debtor's voluntary act, is not a "transfer" and hence not a preference.

Western Tie & Timber Co. v. Brown, 13 A. B. R. 451, 196 U. S. 502: "To give effect, therefore, to the finding that there was no intention on the part of Harrison to prefer, we must consider that the authority given by him to the tie company to collect from the laborers did not give that company the right, or endow it with the option, when it had collected, to retain the money for its exclusive benefit, and to the detriment of the other creditors of Harrison.

"The result of the facts found, then, is this: Harrison sold his goods to the laborers, and agreed with the tie company that that company, when it paid the laborers, should deduct the amount due by the laborers from the wages which the tie company owed them, and, after making the deduction, should remit to Harrison the amount thus deducted, irrespective of any indebtedness otherwise due by Harrison to the tie company. Did this give rise to a voidable preference within the intendment of § 75g and § 60b of the Bankrupt Act?

"In view of the necessary result of the findings which we have previously pointed out, it is, we think, beyond doubt that the agreement was not a voidable preference within the meaning of the statute, since, considering the agreement alone, it brought about no preference whatever."

But, where a bank, by virtue of a "banker's lien," applies the surplus of collateral held for one debt upon another debt held by it, such appropriation does not lack the debtor's voluntary participation and may constitute a preference.⁶⁵

Of course, the transfer may be effected by an agent of the bankrupt, act-

⁶³ *Stern v. Mayer*, 16 A. B. R. 763 (N. Y. Sup. Ct. App. Div.).

⁶⁴ Compare, *McNaboe v. Columbian Mfg. Co.*, 18 A. B. R. 684, 153 Fed. 967 (C. C. A. N. Y.).

⁶⁵ Instance, *In re Belding*, 8 A. B. R. 718 (D. C. Mass.). But compare, *Irish v. Citizens Trust Co.*, 21 A. B. R. 39 (D. C. N. Y.).

ing within the scope of his authority although without the bankrupt's express instruction in the particular instance.⁶⁶

§ 1329½. **Deposits in Bank Offset.**—A bank's appropriation of a deposit to the payment of a loan made to the depositor lacks the element of the debtor's assent and is not a preference: it is not a "transfer."⁶⁷

Lowell v. International Trust Co., 19 A. B. R. 853, 158 Fed. 781 (C. C. A. Mass.): "In no sense, however, is a deposit like the deposit here payment, or intended as payment. This is the first condition of the decision in *New York Bank v. Massey*, and a vital one; because, if a deposit in the usual course of business may be in the nature of a payment, an unlawful preference would necessarily be involved under the circumstances of either *New York Bank v. Massey* or the case at bar, a suggestion of a possibility which the Supreme Court was compelled to negative."

Trust and Savings Bank v. Trust Co., 229 U. S. 435, 30 A. B. R. 624: "As to the \$579.79 we think the right to set off this deposit is established by the principles laid down in *New York County Nat. Bank v. Massey*, supra. Here there was a deposit subject to be checked out by the bankrupt for specific purposes. The money was not placed in the bank with a view to giving it a benefit, except indirectly, because of the deposit. It was subject to Prince's check, and all of it might have been checked out for the purposes intended."

The Supreme Court has even held that where, within the four months before the bankruptcy the depositor gives to the bank checks on his deposit in payment of notes held by the bank, this may be simply a method of giving form to what the law would accomplish in substance, namely, an "offset;" the ruling on this point, however, being unnecessary to the decision in the particular case since the court also found as a fact that the bank had no reasonable cause to believe a preference would result.

Studley v. Bolyston Nat. Bank, 229 U. S. 523, 30 A. B. R. 161: "The case was tried by the referee who sustained the bank's claim of set-off holding that the

66. *Rector v. City Deposit Bk. Co.*, 15 A. B. R. 336, 200 U. S. 405: A clearing house association was held in this case to be the agent of each one of the constituent banks, such that on recalling the checks presented by the bankrupt bank on the day of its failure it held the fund for the benefit of all and could not appropriate it to the use of any particular creditor bank. Compare, *In re Davis*, 9 A. B. R. 670 (D. C. Tex.).

67. Impliedly, *N. Y. Co. Bk. v. Massey*, 11 A. B. R. 42, 192 U. S. 138 (reversing *In re Stege*, 8 A. B. R. 515, 116 Fed. 342, C. C. A.); instance, *West v. Bk. of Lahoma*, 16 A. B. R. 738, 16 Okla. 508.

Obiter, *Bank v. Sundheim*, 16 A. B. R. 866 (C. C. A. Penn.): "This is not the case of a deposit remaining to the credit of a bankrupt's estate at the

time of the filing of the petition in bankruptcy, and which, under certain circumstances, and in the absence of collusion, might be the subject of set-off, but is rather that of a transfer to a bank of a portion of the bankrupt's estate by the bankrupt's own act prior to the bankruptcy, and which was accepted by the bank in partial payment of an unmatured claim, and concerning which transaction a jury has said that the bank had reasonable cause to believe at the time the payment was made that it was accepting a preference." Compare, *In re Davis*, 9 A. B. R. 670, 119 Fed. 950 (D. C. Tex.).

But compare, where the application of the deposits by overdrafts was by agreement, *obiter*, *Tomlinson v. Bk. of Lexington*, 16 A. B. R. 632 (C. C. A. N. Y.).

payments were not transfers; or—if transfers—that the trustee could not recover the money because the bank had no reasonable cause to believe that the payment of the notes would operate as a preference. * * * The case was then brought here by the trustee, who insists that all the payments were transfers—that if the notes charged to the account are not transfers certainly the giving of the three checks for \$5,000 were transfers and that in receiving the same the bank necessarily knew that it was obtaining a preference.

“But if, as found by the referee, the bank had no reasonable cause to believe such transfers would effect a preference, the payments by checks for \$15,000 drawn on the deposit account, are as much protected as if on the same dates similar checks had been given in payment of like amounts due another bank with which the Collver Company kept no account. For there is nothing in the statute which deprives a bank, with whom an insolvent is doing business, of the rights of any other creditor taking money without reasonable cause to believe that a preference will result from the payment. * * *

“In this case the referee found as a fact that the bank had no reasonable cause to believe that a preference would result. The district judge made no finding of fact. * * * The Circuit Court of Appeals made no ruling on this subject, and we, therefore, pass to the consideration of the right of set-off in the light of the finding by the referee, by the district judge, and by the Court of Appeals that the deposits were honestly made in due course of business and without any intent to prefer the bank. * * *

“That section [Bankr. Act, § 68(a)] did not create the right of set-off, but recognized its existence and provided a method by which it could be enforced even after bankruptcy. What the old books called a right of stoppage—what business men call set-off, is a right given or recognized by the commercial law of each of the States and is protected by the Bankruptcy Act if the petition is filed before the parties have themselves given checks, charged notes, made book entries, or stated an account whereby the smaller obligation is applied on the larger. If this set-off of mutual debts has been lawfully made by the parties before the petition is filed, there is no necessity of the trustee doing so. If it has not been done by the parties, then, under command of the statute, it must be done by the trustee. But there is nothing in 68a which prevents the parties from voluntarily doing, before the petition is filed, what the law itself requires to be done after proceedings in bankruptcy are instituted. * * * These were mutual debts, and if on the date the first note became due, the Collver Company had failed to pay it, the bank could have enforced its banker's lien or its right of set-off by applying \$5,000 of the deposits in payment of the note which matured that day, and so on as each of the other notes became due. It cannot have been illegal for the parties on Sept. 12, 20, 30, October 3 and 14, to do what the law would have required the trustee to do in stating the account after the petition was filed on December 16, 1910. No money passed in either instance; for whether the checks for \$5,000 were paid or notes for \$5,000 were charged, was, in either event, a book entry equivalent to the voluntary exercises by the parties of the right of set-off.”

The court below, in the same case, had held that the element of “assent” was not present in such a transaction, since what was done was simply to give form to what the law would have accomplished in substance.

Studley v. Boylston Nat. Bank of Boston, 29 A. B. R. 649, 200 Fed. 249 (C. C. A. Mass.): “It being the fact that the deposits were honestly made, and as also the bankruptcy statutes go beyond the common law, which allows set-off of all debts overdue, in that they also allow set-off of everything due and not due, when brought down to ‘present value’ so far as the interest account is concerned,

it follows that in the present case, as stated in *Lowell v. International Trust Co.*, at page 856 of 19 Am. B. R., at page 784 of 158 Fed., at page 140 of 86 C. C. A., what the bank did was simply to give form to what the law itself would accomplish in substance. We will repeat here what we said there, namely: 'What the International Trust Company did in the case at bar, more than what was done in *New York Bank v. Massey*, was, as we have said, simply to give form to what the law itself accomplished in substance. Moreover, if what was done by the International Trust Company, in distinction from what was done by the creditor in *New York Bank v. Massey*, accomplished a preference, and for that reason was invalid or has been invalidated, the condition prior to the charging up the demand loans would have been restored by force of law, and the deposit would remain with the International Trust Company, precisely as it did in the case before the Supreme Court, and also the law would be left to operate in precisely the same manner. All this, therefore, raises no substantial difference which we can discover to relieve us from the conclusions of the Supreme Court in the case on which the International Trust Company relies.' In applying these broad principles, whether the depositor gave checks against his deposits for notes as they came due or notes which were overdue, or the bank delayed all proceedings until the petition in bankruptcy was filed, and thus evidenced a statutory set-off, was purely a matter of form; and it follows that the decision of the District Court was correct."

But compare, *In re Starkweather & Albert*, 30 A. B. R. 743, 206 Fed. 797 (D. C. Mo.): "The matter may be disposed of upon a broader ground; that the bank did not stand upon its right of set-off. It simply threatened to exercise that right. The matter terminated, however, on the basis of voluntary payments by Starkweather & Albert, in giving checks which were received by the bank as payments. While the distinction seems narrow between a payment resulting from the exercise of the right of set-off and a payment by check given in the presence of the power by the bank to exercise this right of set-off and application, yet the legal distinction exists, in that in the one instance the act is that of the bank, and in the other that of the debtor. The distinction seems to be recognized by the authorities. *Ridge Ave. Bank v. Studheim* (C. C. A. 3rd Cir.), 16 Am. B. R. 863, 145 Fed. 798, 76 C. C. A. 362; *Irish v. Citizens' Trust Co.*, 21 Am. B. R. 39, 163 Fed. 880; *Germania Co. v. Loeb*, 26 Am. B. R. 238, 188 Fed. 289 (C. C. A.). The precise question seems to have been considered by the Supreme Court of the United States in *Traders' Bank v. Campbell*, 14 Wall. 87."

§ 1330. Definition of "Transfer."—Transfer under the peculiar definition of the Bankruptcy Act includes the sale and every other and different mode of disposing of or parting with property, or the possession of property, absolutely or conditionally, as a payment, pledge, mortgage, gift or security.⁶⁸

§ 1331. Payments of Money "Transfers."—The word "transfer" has a broader meaning in this bankruptcy law than has been given it in many jurisdictions.⁶⁹

68. Bankr. Act, § 1 (25). *Clarke v. Rogers*, 228 U. S. 534, 30 A. B. R. 39; *National Newport Bank v. National Herkimer Co. Bank*, 28 A. B. R. 218, 225 U. S. 178.

69. *In re Starkweather & Albert*, 30 A. B. R. 743, 206 Fed. 797 (D. C. Mo.). Compare, *Nat'l Bk. v. Gettinger*, 68 Oh. St. 389: "There is another reason why these creditors can not be com-

"Transfer" under the present Bankruptcy Act includes a payment of money.⁷⁰

Carson, Pirie et al. v. Chic. Title & T. Co., 5 A. B. R. 818, 182 U. S. 438: "It will be observed that payments in money are not expressly mentioned. Transfers of property are, and one of the contentions of appellants is that by 'transfers of property,' payments in money are not intended. The contention is easily disposed of. It is answered by the definitions contained in § 1. It is there provided that "'transfer' shall include the sale and every other and different mode of disposing of or parting with property or the possession of property, absolutely or conditionally, as a payment, pledge, mortgage, gift or security." It seems necessarily to mean that a transfer of property includes the giving or conveying anything of value—anything which has debt-paying or debt-securing power.

"We are not unaware that a distinction between money and other property is sometimes made, but it would be anomalous in the extreme that in a statute which is concerned with the obligations of debtors and the prevention of preferences to creditors, the readiest and most potent instrumentality to give a preference should have been omitted. Money is certainly property, whether we regard any of its forms or any of its theories. It may be composed of a precious metal, and hence valuable of itself, gaining little or no addition of value from the attributes which give it its ready exchangeability and currency. And its other forms are immediately convertible into the same precious metal, and even without such conversion have, at times, even greater commercial efficacy than it. It would be very strange indeed if such forms of property, with all their sanctions and powers, should be excluded from the statute, and the representatives of private debts which we denominate by the general term 'securities' should be included. We certainly cannot so declare upon one meaning of the word 'transfer.' If the word itself permitted such declaration, which we do not admit, the definition in the statute forbids it. 'Transfer' is defined to be not only the sale of property, but 'every other mode of disposing or parting with property.' All technicality and narrowness of meaning is precluded. The word is used in its most comprehensive sense, and is intended to include every means and manner by which property can pass from the ownership and possession of another, and by which the result forbidden by the statute may be

pelled to repay the money so received by them. Said § 6343 (Rev. Stat.) makes no provision as to payments made in contemplation of insolvency or to create a preference, or with intent to hinder, delay or defraud creditors. * * * The word 'payment' is as familiar and as well understood, as the words, 'sale, conveyance, transfer mortgage or assignment' and if the general assembly had intended to legislate against payments, it would have used that word. The legislature having omitted the word 'payment' this court cannot read it into the statute by construction; and especially is this true when we never had any legislation in this State against receiving payment of honest claims, and when such a construction would render the

constitutionality of the act doubtful."

70. West v. Bk. of Lahoma, 16 A. B. R. 733, 16 Okla. 508; Landry v. Andrews, 6 A. B. R. 281, 21 R. I. 597; Knost v. Wilhelm, 2 A. B. R. 471 (Ref. Ohio); Columbus El. Co. v. Worden (In re Fort Wayne El. Corp.), 3 A. B. R. 634, 99 Fed. 400 (C. C. A. Ind.); In re Sloan, 4 A. B. R. 356, 102 Fed. 116 (D. C. Iowa); Boyd v. Lemon, Gale Co., 8 A. B. R. 83, 114 Fed. 647 (C. C. A. Miss.); compare, analogously, In re Riggs Restaurant Co., 11 A. B. R. 508 (C. C. A. N. Y.): This was a case of act of bankruptcy. Obiter, Peterson v. Nash, 7 A. B. R. 181, 112 Fed. 311 (C. C. A. Minn.). Tumlin v. Bryan, 21 A. B. R. 319, 165 Fed. 166 (C. C. A. Ga.), quoted at § 1277, note, and § 1328.

accomplished—a preference enabling a creditor 'to obtain a greater percentage of his debt than any other creditors of the same class.'"

§ 1332. "Transfer" Includes, Also, Pledge, Mortgage, Gift, Security, etc.—The word "transfer" as used in the Bankruptcy Act includes moreover not only a payment of money but also a pledge, a mortgage, a gift or security and every other and different mode of disposing of or parting with property, or the possession of property, absolutely or conditionally.⁷¹ Therefore, a preference may be accomplished by the debtor's pledging his property or part of it, or by mortgaging it or giving it as security for a debt. It is unnecessary to multiply illustrations or citations. Any method of disposing of property to a creditor, or of parting with it or with its possession, even if conditionally, can afford the means of perpetrating a preference. However peculiar the species of property or devious or indirect the method of effecting the transfer, it may result in a preference.⁷²

In *re Belding*, 8 A. B. R. 718 (D. C. Mass.): "An advantage given by the bankrupt to a creditor without present consideration does not cease to be a

71. Bankr. Act, § 1 (25). Instance, *Jones v. Coates*, 28 A. B. R. 249, 196 Fed. 860 (C. C. A. Mo.), decided under the law of Kansas; *Bank of Newport v. Herkimer Co. Bk.*, 225 U. S. 178, 28 A. B. R. 218.

72. See ante, "First Element of Preference,"—"Preferences by Indirect Means," § 1300. Also, see various citations, throughout the subject of Voidable Preferences, involving the different species of transfer. *Stern, Falk & Co. v. Trust Co.*, 7 A. B. R. 305, 112 Fed. 501 (C. C. A. Ky.); In *re Beerman*, 7 A. B. R. 431, 112 Fed. 663 (D. C. Ga.); *Hackney v. Hargreaves Bros.*, 13 A. B. R. 164, 68 Neb. 624.

Instances:

1. **By agreement** of all parties the **placing of a custodian in charge** of a partnership's store **to receive the proceeds** of daily sales and apply them upon a judgment against one of the individual partners, where the judgment and all the other events occurred within the four months preceding the bankruptcy of the partnership and of each of its members: held, a preference. In *re Metzger Toy & Novelty Co.*, 8 A. B. R. 307, 114 Fed. 957 (D. C. Ark.): Proof of knowledge on creditor's part was not necessary, the case being decided before the amendment of 1903.

2. **Depleting the assets by means of a fraudulent scheme** between the assignee for creditors, the partners and some of the creditors involving the

procuring of an order of court in the assignment proceedings ordering a sale, then the bidding in of the property at a low price by the brother of one of the partners for the benefit of the certain creditors and of the firm. *Stern, Falk & Co. v. Trust Co.*, 7 A. B. R. 305, 112 Fed. 501 (C. C. A. Ky.).

3. **Services rendered by debtor to creditor in payment of a debt do not constitute a transfer** of property within the meaning of the law. In *re Abraham Steers Lumber Co.*, 7 A. B. R. 332, 112 Fed. 406 (C. C. A. N. Y.): But was not this a transfer of the chose in action arising from the doing of the work?

4. **Banker's lien upon collateral for other debts** than those for which collateral is expressly pledged. Collateral expressly pledged for presently passing consideration during the four months, is sold and the excess applied upon an old debt. To the extent of such application it is a preference. In *re Belding*, 8 A. B. R. 718 (D. C. Mass.).

5. **Obtaining preference by indirect means:** Third person lending money to debtor to pay creditor, taking chattel mortgage on debtor's property therefor and knowing proposed use of the money, and even taking bond of indemnity from creditor: chattel mortgage void as a preference. In *re Beerman*, 7 A. B. R. 431, 112 Fed. 663 (D. C. Ga.).

Mortgage given for money with which to make a preference is void

preference because it is given in the form of a lien, or of a sale of property without full consideration instead of in the form of a direct payment."

McDonald v. Clearwater R. Co., 21 A. B. R. 182, 164 Fed. 1007 (U. S. C. C. Idaho): "Undoubtedly the assignment under consideration (order by bankrupt seller on buyer, accepted by buyer, assigned to bank) was a 'transfer' of 'property.'"

Obiter, Coder v. Arts, 18 A. B. R. 513, 152 Fed. 943 (C. C. A. Iowa): "The transfer specified in Bankr. Act, § 60 (a), includes a mortgage or a lien voluntarily created by the debtor."

§ 1333. Performance of Labor, Not "Transfer."—But the performance of labor by the debtor is not a "transfer of property" within the meaning of the bankruptcy act.⁷³

§ 1333½. Embezzlements from Bankrupt Corporations.—Where money is embezzled or stolen from a bankrupt corporation, the element of voluntary action on the part of the debtor is lacking, and there is no "transfer," hence no preference.⁷⁴

§ 1334. When "Transfer" Consummated, Where Recording "Necessary."—In cases of transfers effected by instruments that require filing or recording to impart notice, the consummation of the transfer, so far as creditors are concerned, it would seem from principle, is not accomplished until the instrument is filed or recorded.⁷⁵

[Before Amendment of 1910 to § 60 (b).] *Matthews v. Hardt*, 9 A. B. R. 383 (N. Y. Sup. Ct. App. Div.): "The trend of the decisions in the United States Supreme Court under the recent Bankruptcy Act upon the subject of the date of the transfer, is in support of the view that with respect to an instrument of transfer, it is the time when such instrument is recorded, or when possession is

although for presently passing consideration to the mortgagor, the mortgagee taking a bond of indemnity from the creditor therefor. In *re Beerman*, 7 A. B. R. 431, 112 Fed. 663 (D. C. Ga.).

Obtaining preference by indirect means: *Hackney v. Hargreaves Bros.*, 13 A. B. R. 164, 68 Neb. 624.

6. **Orders drawn by bankrupt on third persons** for debts owing operate, when accepted and assigned, as transfers sufficient to constitute preferences. *McDonald v. Clearwater R. Co.*, 21 A. B. R. 182, 164 Fed. 1007 (U. S. C. C. Idaho). Also, when they amount to assignments of the fund. In *re Hines*, 16 A. B. R. 495, 144 Fed. 543 (D. C. Penn.).

73. In *re Abraham Steers Lumber Co.*, 6 A. B. R. 315 (D. C. N. Y.), affirmed in 7 A. B. R. 332, 112 Fed. 406). See also, ante, "First Element of Preference," § 1280. Compare, to effect that contract to labor is not "property," transferable, analogously. In *re Home*

Security Co., 17 A. B. R. 181 (D. C. Ala.).

Compare, analogously to same effect, In *re Thaw*, 24 A. B. R. 759, 180 Fed. 419 (D. C. Pa.), quoted at § 2747.

74. Instance, though placed rather on ground of lack of reasonable cause for belief on creditor's part, *McNaboe v. Columbian Mfg. Co.*, 18 A. B. R. 684, 153 Fed. 967 (C. C. A. N. Y.).

75. But compare, *Bradley, Clark & Co. v. Benson*, 13 A. B. R. 170, 100 N. W. 670 (Minn.); *First Nat'l Bk. v. Connett*, 15 A. B. R. 662, 142 Fed. 33 (C. C. A. Mo.), quoted at § 1379; also, contra, *Claridge v. Evans, Evans v. Claridge* (Wis.), 118 N. W. 198, quoted at § 1379.

Compare, where Pennsylvania law is said to declare a mortgage "not a lien" until recorded. In *re Dundore*, 26 A. B. R. 100 (D. C. Pa.).

[Before Amendment of 1910 to § 60 (b).] Contra, *Dougherty v. First National Bank*, 28 A. B. R. 263, 197 Fed. 241 (C. C. A. Ohio).

taken or notice is otherwise brought home to the creditors of the bankrupt that is controlling."

[Before Amendment of 1910 to § 60 (b).] Page 782. *McElvain v. Hardesty*, 22 A. B. R. 320, 169 Fed. 31 (C. C. A. Mo.): "* * * the effect of the transfer to McElvain is to be judged as if made on the 7th day of July, 1905, when it was recorded. If C. & C. were then insolvent and the effect of the enforcement of the transfer was to enable McElvain to obtain a greater percentage of his debt than any other of their simple contract creditors, the transfer constituted a preference within the meaning of the bankruptcy law. * * * As, for the purposes of this case, the transfer is to be treated as made on the date the agreement was recorded, so the transferee's belief or cause for belief concerning it must relate to that time."

[Before Amendment of 1910 to § 60 (b).] In *re Hickerson*, 20 A. B. R. 682, 162 Fed. 345 (D. C. Idaho): "By the Amendment of 1903, it is provided that, to constitute a preference, the period during which the transfer is made shall not expire until four months after the date of the recording or registering of the transfer, if by law such recording or registering is required. The mortgage 'transfer' must therefore be deemed to have been made on the 11th day of February 1907, only five days before the filing of the petition in bankruptcy."

[Before Amendment of 1910 to § 60 (b).] *Contra*, *Rogers v. Page*, 15 A. B. R. 506, 140 Fed. 596 (C. C. A. Penn.): "The preference over other creditors was given when the mortgage was executed and delivered. It follows that if the defendant has shown an appropriation of a part of the purchase price of the bankrupt's coal land in satisfaction of a valid indebtedness secured by an unrecorded lien made, accepted, and held in good faith, more than four months before the filing of the mortgagor's voluntary petition in bankruptcy, he may escape a decree against him to that extent."

[Before Amendment of 1910 to § 60 (b).] *Ragan v. Donovan*, 26 A. B. R. 311, 189 Fed. 138 (D. C. Ohio): "The court is justified, we think, in holding that the interpretation placed upon the language of § 60 paragraph (a) read in connection with § 3, paragraph (b) of the Bankruptcy Act by the cases of *English v. Ross* (D. C. Pa.), 15 A. B. R. 370, 140 Fed. 630, *Loeser v. Savs. Bk.* (C. C. A. 6th Cir.), 17 A. B. R. 628, 148 Fed. 975, and *In re Becklans* (C. C. A. 7th Cir.), 24 A. B. R. 380, 177 Fed. 141, should be applied to a transaction where deeds of realty are involved, as in this case, and that we should hold that the preference, manifestly attempted in behalf of the bank should be referred for date to the time of filing the deeds."

§ 1334 1/10. Conditional Sales, Not "Transfers."—A conditional sale, unless a mere disguise, is not a "transfer" out of the insolvent fund, but is a reservation of title, and therefore cannot be a preference;⁷⁶ a fortiori, the recording of it could not operate as a transfer, nor could the failure to record it effect a transfer of the title to the conditional vendee.⁷⁷

Conditional sales are not "transfers" and therefore cannot constitute preferences.

⁷⁶ Compare ante, § 1244, and post, § 1372½; compare, perhaps in point though only impliedly, *In re Hutchins*, 24 A. B. R. 647, 179 Fed. 864 (D. C. N. Y.). And delay for six months in executing a formal lease or conditional sale contract will not invalidate the transaction [unless the property come

into the custody of the bankruptcy court in the meantime so that such custody will operate as a levy under Bankr. Act § 47 (a)]. In *re Hutchins*, 24 A. B. R. 647, 179 Fed. 864 (D. C. N. Y.).

⁷⁷ *Bradley, Clark & Co. v. Benson*, 13 A. B. R. 170, 100 N. W. 670 (Minn.).

Deere Plow Co. v. Farmer Store Co., 31 A. B. R. 156 (Wis.): "The contract in question is clearly a conditional sale within the rule of the cases of this and other courts, and, being free from actual fraud, must be held valid and effective. * * * The respondent's contention that the transaction embraced in this contract constituted an unlawful preference under section 60 of the Bankruptcy Act must also fail; the bankrupt transferred no estate in any of this property, nor was anything done by way of securing any antecedent debt of the bankrupt so as to invalidate the transfer within the provisions of this provision of the Bankruptcy Act."

Big Four Implement Co. v. Wright, 31 A. B. R. 125, 207 Fed. 535 (C. C. A. Kan.): "These being contracts of conditional sale, there is no foundation for the claim that the filing of them within four months of the bankruptcy constituted a preference. There could be no preference without a transfer by the bankrupt of his property. If there were any transfer in this case it is evidenced by these instruments dated Dec. 8, 1910, and Jan. 23, 1911. But they transferred no property of Bell. They expressly refrained from transferring any to him."

In re Farmer's Co. of Barlow (No. 1), 30 A. B. R. 187, 202 Fed. 1005 (D. C. N. Dak.): "The trustee's main reliance, however, is that the granting of the petition of the plow company would secure to it a preference over the other creditors of the estate. By section 60a of the Bankruptcy Act, the contract must be judged as of the date of its filing. Because that date fell within four months of the filing of the petition, the referee held that to enforce the provisions of the conditional sale contract would secure to the plow company a preference. I am unable to concur in that view for two reasons: First, the bankrupt never had any title to the property. The title was, by the terms of the contract, reserved to the seller. By the great weight of authority such a reservation is entirely valid. *Harkness v. Russell*, 118 U. S. 663, 7 Sup. Ct. 51, 30 L. Ed. 285; *Williston on Sales*, 324. The only right in the property which the bankrupt secured was the right of possession. The property was not, therefore, the property of the bankrupt, and the contract could not in any aspect amount to a transfer of 'its property' within the meaning of §§ 60a and 60b. Second. The reservation of title in the contract does not amount to a transfer from the buyer to the seller. It is simply a reservation of title by the seller to himself as one of the conditions upon which possession of the property is transferred to the buyer. The contract cannot, therefore, be held to amount to a 'transfer' of property from the buyer to the seller. It has sometimes been said by courts and text-writers that a conditional sale amounts to a sale of the property with a mortgage back. That is not its character, and nothing but confusion can result from attempting to describe a conditional sale in terms of a mortgage. If the purchaser pays down a part of the purchase price at the time of the sale, or at a subsequent date before the seller attempts to enforce the condition, it is quite true that the buyer has an equitable interest in the property by reason of the payments. When the facts present such a case, it may be that a court of bankruptcy will find a way to protect the equitable interest of the bankrupt against forfeiture. *Williston on Sales*, § 579. The present case, however, presents no such question, for the evidence shows, and the referee has found, that the amount now due on the contract considerably exceeds the purchase price of the property here involved."

Baker Ice Machine Co. v. Bailey, 31 A. B. R. 593 (C. C. A. Kans.): "The district court treated the conditional sale contract as a transfer effective May 15th, 1912, the date of its filing to secure an existing indebtedness of that this date being within four months of the time of the filing of the voluntary petition in bankruptcy—July 11, 1912—the transfer was void as a preference. We think

this was error and that the error arose from holding that the conditional sale contract operated as a transfer."

Big Four Implement Co. v. Wright, 31 A. B. R. 125, 207 Fed. 535 (C. C. A. Kans.): "These being contracts of conditional sale, there is no foundation for the claim that the filing of them within four months of bankruptcy constitute a preference. There could be no preference without a transfer by the bankrupt of his property. If there was a transfer in this case, it is evidenced by the instrument dated December 8, 1910, and January 23, 1911. But they transferred no property of Bell. They expressly refrained from transferring any to him."

Hart v. Emmerson-Brantingham Co., 30 A. B. R. 218, 203 Fed. 60 (D. C. Mo.): "The return of the goods cannot properly be treated as a preferential transfer, for the defendant took back the property under the assertion of a paramount title and did not take it as a creditor for application upon a debt."

§ 1334^{1/4}. Where Recording "Not Necessary."—As noted elsewhere⁷⁸ local or general law, as distinguished from bankruptcy law, determines when a "transfer" shall be considered as consummated where recording is not "necessary." Thus, in the absence of a recording statute to cover the case, general law will control as to the time an assignment of a chose in action will be considered as consummated.

In *re Wilson*, 23 A. B. R. 814 (D. C. Hawaii): "There is no requirement in the Hawaiian statutes that bills of sale of chattels must be recorded in order to be valid. * * * In view of these facts and considerations, I find that the assignments in question were not complete until notice thereof was given to the county of Kauai, which notice, in both cases, was within four months of the date when the petition for adjudication was filed. But as it appears from all the evidence that the transfers were initiated before the four months began to run, were such transfers preferences under the Bankruptcy Act, § 60a, which makes a transfer by an insolvent person within the four months, a preference? Does the act of the insolvent, in order to make it a preference, require its effectuation by notice according to the above finding? I think not. The transfer is complete when the assignment is made, so far as the assignor can complete it. These transfers, therefore, not having been made within the four months, are not preferences; and this would seem to require the affirmative answer to the submitted question." Quoted also at § 1275.

§ 1334^{1/2}. Amendment of 1910—Transfer Consummated at Date of Recording.—The Amendment of 1910 to § 60b adopts the date of recording, where recording is required by State law, as the effective date of the consummation of the transfer.⁷⁹

⁷⁸. See ante, §§ 1139, 1275; post, § 1373.

⁷⁹. See post, § 1379^{1/2}. See *Bankr. Act*, § 60b, as amended in 1910: "If a bankrupt shall have procured or suffered a judgment to be entered against him in favor of any person or have made a transfer of any of his property, and if, at the time of the transfer, or of the entry of the judgment, or of the recording or registering of the trans-

fer if by law recording or registering thereof is required, and being within four months before the filing of the petition in bankruptcy or after the filing thereof and before the adjudication, the bankrupt be insolvent and the judgment or transfer then operate as a preference, and the person receiving it or to be benefited thereby, or his agent acting therein, shall then have reasonable cause to believe that the

§ 1335. "Procuring or Suffering" Judgment.—Where the preference is not by way of a "transfer," it is essential, at least, that the bankrupt must have "procured or suffered" the creditor to obtain a judgment, under which levy or other seizure was made.⁸⁰

In *re* Nusbaum, 18 A. B. R. 598, 152 Fed. 835 (D. C. N. Y.): "When the alleged bankrupt * * * being insolvent, voluntarily confessed judgment in favor of certain of his creditors * * * with the intent to prefer such creditors over his other creditors, and permitted them, as he knew they would and as they did, to issue executions thereon and levy upon and sell all his property by virtue thereof, and put the proceeds of such sale of such property in their pockets in payment and satisfaction of their respective debts, as he knew they would and intended they should, be transferred while insolvent * * * with intent to prefer the creditors in whose favor he confessed such judgments, it was not a sale by him in form, but it was a different mode of disposing of or parting with property, or the possession of property absolutely, and 'as security' first, and second 'as a payment' to such preferred creditors. * * * It was a 'transfer' within the plain definition of the term found in cl. 25 of § 1 of the act."

Grant v. National Bank of Auburn, 28 A. B. R. 712, 197 Fed. 581 (D. C. N. Y.): "All this was done when the defendant in such judgment and execution,

enforcement of such judgment or transfer would effect a preference, it shall be voidable by the trustee and he may recover the property or its value from such person."

80. Instance, In *re* Metzger Toy & Novelty Co., 8 A. B. R. 307, 114 Fed. 957 (D. C. Ark.): This case does not appear clearly to involve the question of the suffering or procuring of a judgment, but is rather an authority upon the matter of a preference by way of "transfer."

Instance, In *re* Heinsfurter, 3 A. B. R. 109, 97 Fed. 198 (D. C. Iowa): Retaining possession of property under writ of replevin although application for surrender under claim of fraud disallowed by bankruptcy court.

Instance, In *re* Collins, 2 A. B. R. 1 (Ref. Iowa): Seeing certain creditors bringing suit and obtaining liens thereby which necessarily result in such creditors obtaining preferences is a "permitting" of preferences.

Instance, In *re* English, 11 A. B. R. 674, 127 Fed. 940 (C. C. A. N. Y.): Part of judgment valid as simply declaratory of rights given before the four months: rest of judgment void as creating liens and transferring property preferentially within the four months. Partnership, more than four months before bankruptcy, transfers, in full payment, to one creditor a part of its assets: dissolution proceedings are instituted, ending in judgment within the four months period, affirming the va-

lidity of the transfer and ordering certain of the general creditors to be paid out of the residue: Held, judgment as to validity of transfer unimpeachable (because simply an affirmation of a previous transfer) but as to ordering payment of certain creditors to the exclusion of others, a preference within four months by "suffering" a judgment to be entered.

Inferentially, but obiter, In *re* Portersfield, 15 A. B. R. 11, 138 Fed. 192 (D. C. W. Va.): Statutory suits to set aside fraudulent or preferential transfers operating to give certain creditors or certain classes of creditors on recovery, different rights or priorities in the proceeds than those prescribed by the Bankruptcy Act may create voidable preferences.

Suffering a judgment whose necessary effect is to create a preference, is the suffering of the preference, In *re* Collins, 2 A. B. R. 1 (Ref. Iowa).

An attachment in New York is neither a "judgment" nor a "transfer" and need not be surrendered, In *re* Schenkein & Coney, 7 A. B. R. 162, 113 Fed. 421 (Ref. N. Y.).

Instance, *Moore v. J. M. H. Smith Sons*, 30 A. B. R. 413, 205 Fed. 431 D. C. N. Y.).

Instance [surety on government contract advancing money to meet payroll and taking cognovit note therefor and levying execution same day, yet held preference], *United Surety Co. v. Iowa Mfg. Co.*, 24 A. B. R. 726, 179 Fed. 55 (C. C. A. Mo.).

the Cayuga Construction Company, was insolvent, which fact was known to both the parties, and the judgment was given as a means of effecting a preference and received as such, that is, as a means of transferring the property of the Cayuga Construction Company, or its proceeds, to the said National Bank of Auburn, in satisfaction or payment, so far as it would go, of a prior debt."

"Judgment" probably applies to any court proceedings whereby the estate is depleted; thus, to a fraudulent scheme under cloak of court orders whereby the estate is depleted, as where an assignee in insolvency was to sell under order of court at a purposely low figure to the brother of one partner, who was to pay certain creditors 50 per cent of their claims, the balance to the debtor firm.⁸¹

§ 1336. Warrants of Attorney to Confess Judgment, Continuing Consents.—Judgment levies within the four months period on warrants of attorney to confess judgment executed before the four months, constitute continuing assent or acquiescence.⁸² But "continuing consent" is not necessary; mere passive nonresistance is sufficient.⁸³

§ 1337. Debtor's Voluntary Action Not Implied in Cases of Preferences by Way of Judgments.—The debtor's positive action perhaps is not implied in case the preference be by way of legal proceedings. Mere passive nonresistance may be all that is requisite.⁸⁴

Contra, *Johnson v. Anderson*, 11 A. B. R. 302, 70 Neb. 233: "In order to constitute a preference, the debtor must do some act to facilitate the proceedings; submissive inactivity is not enough. * * * It is certainly competent for a creditor to institute an attachment suit against a bankrupt, obtain judgment by default, and sell the attached property; and, unless the bankrupt does some act by which he has participated in some way in the act of the creditor, the preference otherwise acquired is a valid preference as against other creditors."

Contra, under law of 1867, *Wilson v. City Bk.*, 17 Wall. 488: "Something more than passive nonresistance of an insolvent debtor, to regulate judicial proceedings in which a judgment and levy on his property are obtained, when the debt is due, and he is without just defense to the action, is necessary, to show a preference of a creditor, or a purpose to defeat or delay the operation of the Bankrupt Act."

⁸¹ In re Stern, Falk & Co., 7 A. B. R. 305, 112 Fed. 501 (C. C. A. Ky.).

⁸² *Grant v. Nat. Bank*, 28 A. B. R. 712, 197 Fed. 581 (D. C. N. Y.), quoted at § 1335; *Wilson Bros. v. Nelson*, 7 A. B. R. 142, 183 U. S. 191; impliedly, In re Huffman, 1 A. B. R. 587 (Ref. Penn.); analogously, In re Moyer, 1 A. B. R. 577, 97 Fed. 324 (D. C. Penn.). See cases cited under "Third Act of Bankruptcy," § 135.

⁸³ See cases cited ante, under "Third Act of Bankruptcy," § 136. *Wilson v. Nelson*, 183 U. S. 191, 7 A. B. R. 142.

⁸⁴ See cases cited ante, under "Third

Act of Bankruptcy," § 135; In re Gallagher, 6 A. B. R. 255 (Ref. Mass.); (Act of bankruptcy) *Bogen & Trummel v. Protter*, 2 A. B. R. 288, 129 Fed. 533 (C. C. A. Ohio); apparently probut consistent with contra, *Wilson v. Nelson*, 183 U. S. 191, 7 A. B. R. 142.

Compare, instance, [surety on government contract advancing money to meet payroll and taking judgment note therefor and levying execution on the same day, yet held to be a preference as an act of bankruptcy]. *United Surety Co. v. Iowa Mfg. Co.*, 24 A. B. R. 726, 179 Fed. 55 (C. C. A. Mo.).

Contra, under law of 1867, *Brown v. Jefferson County Nat'l Bk.* (C. C. A. N. Y.), 9 Fed. 258: "The mere existence of a desire on the part of a debtor, however strong such desire, that a particular creditor may succeed by suit, judgment, execution and levy in obtaining a preference over other creditors, so that such preference may be maintained, even as against proceedings in bankruptcy which may be subsequently commenced, is not sufficient to establish that the debtor procured or suffered his property to be taken on legal process, with intent to prefer such creditor, if the proceedings of the creditor were the usual proceedings in a suit, unaided by any action of the debtor, either by facilitating the proceedings as to time or method, or by obstructing other creditors who otherwise would obtain priority."

§ 1338. Payment of Proceeds of Execution Sale to Creditor Sufficient without Debtor's Voluntary Action.—The payment of the proceeds of an execution or attachment sale to the levying creditor, if otherwise preferential, is none the less a preference because of the lack of the debtor's voluntary act.⁸⁵

§ 1339. Fifth Element of a Preference.—Where the preference is by way of a transfer, the transfer must have been made by the transferror to satisfy a debt in whole or in part and the property must have been sought to be applied on a debt. Preference, by way of transfer, implies an intent of the transferror to apply the property on a debt, or obligation.

§ 1340. Intent to Apply on Debt to Be Distinguished from Intent to Prefer.—By this is not meant that the transferee must be proved to have intended the transfer as a preference; intent to pay a debt and intent, by paying it, to prefer, are wholly different matters.

Property of the debtor not transferred to apply on a debt, does not give rise to a preference, although it may be used as an offset. Thus, the retaining, to apply on a creditor's own claim against a bankrupt storekeeper, funds deducted by arrangement from the wages of the creditor's employees to pay for supplies furnished the employees by the storekeeper, has been held an offset (although an improper one in this case) and not a preference, since the element of the debtor's application of the payment on the debt was lacking.⁸⁶

§ 1340½. Transfer to Creditor but Not to Apply on Indebtedness.—Though the person to whom the transfer is made be also a creditor, yet the transfer will not be a preference if it is not made to apply upon some debt existing between them. Thus, where the wife of a bankrupt is a bona

⁸⁵ See, impliedly, cases cited under "Third Act of Bankruptcy," § 135, et seq.; contra, *Johnson v. Anderson*, 11 A. B. R. 302, 70 Neb. 233; contra (under law of 1867), *Wilson v. City Bk.*, 17 Wall. 488; contra (under law of

1867), *Brown v. Jefferson County Bk.*, 9 Fed. 258 (C. C. A. N. Y.). Also, compare, post, § 1478.

⁸⁶ *Western Tie & Timber Co. v. Brown*, 13 A. B. R. 447, 196 U. S. 502 (reversing 12 A. B. R. 111).

fide creditor, money given to her by the bankrupt to defray family expenses does not constitute a preference.⁸⁷

But this proposition must not be thought to support the doctrine that a payment upon one debt is not a preference upon other debts existing between the parties. The payment must not be made in reduction of any part of the aggregate indebtedness between the parties, else it will not be lacking in this element of a preference, for the whole state of the indebtedness between the parties is to be taken into account. The doctrine of this section simply is that a transfer made for a different purpose from that of the payment of a debt cannot constitute a preference.

§ 1341. Bankrupt's Deposit in Bank.—Thus, a bankrupt's deposit in bank, so long as it was made as a general deposit subject to check, is not a preference and may be offset: the relation is that of debtor and creditor, and the mutual debts may be offset, the depositing not having been made to pay a debt.⁸⁸

N. Y. County Nat'l Bk. v. Massey, 11 A. B. R. 42, 192 U. S. 138: "The money deposited becomes a part of the general fund of the bank, to be dealt with by it as other moneys, to be lent to customers, and parted with at the will of the bank, and the right of the depositor is to have this debt repaid in whole or in part by honoring checks drawn against the deposits. It creates an ordinary debt, not a privilege or right of a fiduciary character. * * *

"As we have seen, a deposit of money to one's credit in a bank does not operate to diminish the estate of the depositor, for when he parts with the money he creates at the same time, on the part of the bank, an obligation to pay the amount of the deposit as soon as the depositor may see fit to draw a check against it. It is not a transfer of property as a payment, pledge, mortgage, gift or security. It is true that it creates a debt, which, if the creditor may set it off under § 68, amounts to permitting a creditor of that class to obtain more from the bankrupt's estate than creditors who are not in the same situation, and do not hold any debts of the bankrupt subject to set-off. But this does not, in our opinion, operate to enlarge the scope of the statute defining preferences so as to prevent set-off in cases coming within the terms of § 68a. If this argument were to prevail, it would, in cases of insolvency, defeat the right of set-off recognized and enforced in the law, as every creditor of the bankrupt holding a claim against the estate subject to reduction to the full

⁸⁷. *Neumann v. Blake*, 24 A. B. R. 575, 178 Fed. 916 (C. C. A. Mo.).

⁸⁸. See, also, ante, §§ 1180, 1297; *Germania Savings & Trust Co. v. Loeb*, 25 A. B. R. 238, 188 Fed. 285 (C. C. A. Tenn.); *Studley v. Boyleston Nat. Bank*, 229 U. S. 523, 30 A. B. R. 161, quoted at § 1329½; impliedly, *Irish v. Citizens Trust Co.*, 21 A. B. R. 39 (D. C. N. Y.), quoted ante, § 1328; instance of offset of deposit, *Booth v. Prete*, 22 A. B. R. 579, 81 Conn. 636, 71 Atl. 938; *In re Ph. Semmer Glass Co.*, 11 A. B. R. 665 (D. C. N. Y.); *In re Elsasser*, 7 A. B. R. 215 (Ref. Penn.); *In re Geo. M. Hill*, 12 A. B. R. 221 (C. C. A. Ills.);

In re Scherzer, 12 A. B. R. 451, 130 Fed. 631 (D. C. Iowa); *West v. Bk. of Lahoma*, 16 A. B. R. 738, 16 Okla. 508; *obiter*, *Bk. v. Sundheim*, 16 A. B. R. 866 (C. C. A. Pa.); compare, *In re Davis*, 9 A. B. R. 670 (D. C. Tex.).

But see for singular misapplication of the rule, where the application of deposits to pre-existing overdrafts within the four months by **agreement** was held not to be a preference; *obiter*, *Tomlinson v. Bank of Lexington*, 16 A. B. R. 632 (C. C. A. N. Car.): The case is, however, *obiter*, for "reasonable cause for belief" was lacking.

amount of a debt due the bankrupt receives a preference in the fact that to the extent of the set-off he is paid in full."

Lowell v. International Trust Co., 19 A. B. R. 853, 158 Fed. 781 (C. C. A. Mass.): "Undoubtedly the District Court, in ordering a verdict for the defendant, felt compelled thereto by *New York Bank v. Massey*, * * * We are unable to perceive how we can substantially distinguish the two cases. * * * The plaintiff calls to our attention *Traders' Bank v. Campbell*, 14 Wall. 87, * * * but that was distinguished in *New York Bank v. Massey*, as follows: * * * 'In *Traders' Bank v. Campbell*, * * * the right of set-off was not relied upon, but a deposit was seized on a judgment which was a preference.' * * * In other words, the bank clearly did not rely at all on its relations to the bankrupt as its customer, but it put itself entirely on its rights as an execution creditor, which rights, as the law then stood, were under the circumstances ineffectual. The plaintiff also urges on us that, in *New York Bank v. Massey*, the bank took no action formally or otherwise, but merely left it to the law to offset the deposit made by the bankrupt against his indebtedness, while in the case at bar we must accept the statement that the defendant charged up its demand loans against the deposit, or, in other words, went through the formalities of certain alleged journal entries. This, however, was ineffectual either way, whether to benefit or prejudice the International Trust Company. It only gave expression to what the law itself would accomplish, that is, it cleaned up the set-off and left it where the law itself would have left it. At law, it takes two parties to accomplish an effectual payment, both a payor and a payee. Sometimes, of course, the law appropriates moneys in payment, or permits the creditor to do it; but that is in consequence of some express or implied understanding between the parties. In such instances an intention on the part of both parties to make payment on some indebtedness underlies what the law accomplishes, and the law is called in only because, while payment is intended, the particular item of indebtedness to which it shall be appropriated is not specifically pointed out. In no sense, however, is a deposit like the deposit here payment, or intended as payment. This is the first condition of the decision in *New York Bank v. Massey*, and a vital one; because, if a deposit in the usual course of business, may be in the nature of a payment, an unlawful preference would necessarily be involved under the circumstances of either *New York Bank v. Massey* or the case at bar, a suggestion of a possibility which the Supreme Court was compelled to negative."

Studley v. Boylston Nat. Bank of Boston, 29 A. B. R. 649, 200 Fed. 249 (C. C. A. Mass.): "Of course, to be within the rule of the cases cited, good faith must exist, and there must be no deposits made after insolvency threatens, wholly or especially for the purpose of enabling a bank to secure an advantage over other creditors. In this case it is plain there was no such intention; and it is also plain that the deposits were honestly made, so that, within the somewhat artificial rule in *Bank v. Massey*, as stated in the opinion of Mr. Justice Day in behalf of the court, at page 147 of 192 U. S., at page 46 of 11 Am. B. R. at page 201 of 24 Sup. Ct. (48 L. Ed. 380): 'A deposit of money to one's credit in a bank does not operate to diminish the assets of the depositor.' It being the fact that the deposits were honestly made, and as also the bankruptcy statutes go beyond the common law, which allows set-off of all debts overdue, in that they also allow set-off of everything due and not due, when brought down to "present value" so far as the interest account is

concerned, it follows that in the present case, as stated in *Lowell v. International Trust Co.*, at page 856 of 19 Am. B. R., at page 784 of 158 Fed., at page 140 of 86 C. C. A. what the bank did was simply to give form to what the law itself would accomplish in substance. We will repeat here what we said there, namely: 'What the International Trust Company did in the case at bar, more than what was done in *New York Bank v. Massey*, was, as we have said, simply to give form to what the law itself accomplished in substance. Moreover, if what was done by the International Trust Company, in distinction from what was done by the creditor in *New York Bank v. Massey*, accomplished a preference, and for that reason was invalid or has been invalidated, the condition prior to the charging up the demand loans would have been restored by force of law, and the deposit would remain with the International Trust Company, precisely as it did in the case before the Supreme Court, and also the law would be left to operate in precisely the same manner. All this, therefore raises no substantial difference which we can discover to relieve us from the conclusions of the Supreme Court in the case on which the International Trust Company relies:

"In applying these broad principles, whether the depositor gave checks against his deposits for notes as they came due or notes which were overdue, or the bank delayed all proceedings until the petition in bankruptcy was filed, and thus evidenced a statutory set-off, was purely a matter of form; and it follows that the decision of the District Court was correct."

But where the deposit was itself made precisely for the purpose of permitting checks to be drawn to create preferences, the situation would be different.⁸⁹

Likewise, where a bank, being the largest creditor, acted as agent of a lender who loaned the insolvent money, which was deposited in the bank and later "offset" or appropriated by the bank, the loan being on a demand note, a chattel mortgage given to the lender at the time has been held voidable as a preference.⁹⁰

And a deposit will be held to constitute a preference where it appears that the bank induced the making of it with the intention and purpose of applying it on an indebtedness owing to the bank by the depositor;⁹¹ and where a bank required a depositor to give it a check on his account in payment of notes not then due, the transaction was held to constitute a preference.⁹²

Again an intention to accept a preference has been held to exist where a deposit was accepted after the bank had ordered that no more certifications should be made, the order having been made because of the bank's knowledge of impending insolvency;⁹³ but the depositor must have intended to have applied the deposit on the debt owing to the bank, else it could not

^{89.} *Irish v. Citizens Trust Co.*, 21 A. B. R. 39 (D. C. N. Y.); *Studley v. Boylston Nat. Bank*, 229 U. S. 523, 30 A. B. R. 161, quoted at § 1329½.

^{90.} *In re Lynden Mercantile Co.*, 19 A. B. R. 444, 156 Fed. 713 (D. C. Wash.).

^{91.} *Schmidt v. Bank of Commerce*, 25 A. B. R. 904 (Supreme Court N. Mex.).

^{92.} *Shale v. Farmers' Bank*, 25 A. B. R. 888 (Kans.).

^{93.} *Ernst v. Mechanics' Bank*, 29 A. B. R. 289, 201 Fed. 664 (C. C. A. N. Y.).

have been held to be a preference, though it might have been held to be a trust fund.

However, it has been held that checks deposited for collection on the same day, shortly before the bankruptcy petition was filed, but not collected until the next day, may not be offset.⁹⁴

And an offset of the deposit may be allowed even though the notes or other obligations owing to the bank are not yet due,⁹⁵ so long as it is a true offset and not an application of the deposit on the debt by the debtor.

But collusion between the depositor and the bank to make the facts appear as if there were no consent destroys the right of offset.⁹⁶

In *re Wright-Dana Hardware Co.*, 31 A. B. R. 192, 207 Fed. 636 (D. C. N. Y.): "In the case now before this court there was a parting with the bankrupt's property, first a sale and collection of accounts and then a deposit for the benefit of the bank and for the very purpose of having the deposits held by the bank and applied on the notes held by it. The evidence here does show 'collusions with a view to create a preferential transfer of the bankrupt's property to the bank' and no other conclusion is possible. But as to the deposits prior to January 1, 1912, and the application of the deposits on the notes held by the bank, we have a different situation and a different state of facts. As to those transactions it is a question whether they constitute preferential payments or mere offsets. Prior to January 1, 1912, the business of the company was being conducted in the usual manner. Sales were made the money collected and placed in the bank in the usual course."

§ 1342. Sixth Element of a Preference.—The debtor must have been insolvent at the time of the transfer or other voluntary appropriation of property. Preference implies insolvency of the debtor. Of course there can be no preference among creditors if the debtor is solvent, for then he can pay all his debts in full.⁹⁷

94. *Moore v. Third Nat'l Bank of Phila.*, 24 A. B. R. 568, Pa. Sup. Ct., quoted at § 1297.

95. *Germania Sav. & Trust Co. v. Loeb*, 26 A. B. R. 238, 188 Fed. 285 (C. C. A. Tenn.).

96. *Walsh v. First Nat'l Bank*, 29 A. B. R. 118, 201 Fed. 522 (C. C. A. Ky.), quoted at § 1297.

97. Bankr. Act, § 60 (a); *Cullinane v. State Bk.*, 12 A. B. R. 779, 123 Iowa 340; *In re Chappell*, 7 A. B. R. 608, 113 Fed. 545 (D. C. Va.); *In re Alexander*, 4 A. B. R. 37, 102 Fed. 464 (D. C. Ga.); *In re Clifford*, 14 A. B. R. 281, 136 Fed. 475 (D. C. Iowa); also, see cases cited in the following paragraphs, under "Sixth Element of a Preference." *Naylon & Co. v. Christiansen Co.*, 19 A. B. R. 789, 158 Fed. 290 (C. C. A. Mich.); *Tumlin v. Bryan*, 21 A. B. R. 319, 165 Fed. 166 (C. C. A. Ga.); *In re Lynn Camp Coal Co.*, 22 A. B. R. 60, 168 Fed. 998 (D. C. Ky.); *In re Neill-Pineknay-*

Maxwell Co., 22 A. B. R. 401, 170 Fed. 481 (D. C. Pa.); *Taylor v. Nichols*, 23 A. B. R. 310, 134 App. Div. (N. Y.) 787; *Harder v. Clark*, 23 A. B. R. 756 (City Court of New York); *Newman v. Dry Goods Co.*, 31 A. B. R. 399 (Kansas City Court of Appeals), quoted at §§ 1407 and 1277 note; *Sparks v. Marsh*, 24 A. B. R. 280, 177 Fed. 739 (D. C. Ark.); impliedly, *Alexander v. Redmond*, 24 A. B. R. 620, 180 Fed. 92 (C. C. A. N. Y.); *Stern v. Paper Co.*, 28 A. B. R. 592, 198 Fed. 642 (C. C. A. N. Dak.); *Ogden v. Reddish*, 29 A. B. R. 531, 200 Fed. 977 (D. C. Ky.); *In re Starkweather & Albert*, 30 A. B. R. 743, 206 Fed. 797 (D. C. Mo.).

Estoppel from Claiming Insufficiency of Proof of Indebtedness by Previously Obtaining Court's Favorable Ruling against Admissibility of Same Evidence.—*Gering v. Leyda*, 26 A. B. R. 137, 186 Fed. 110 (C. C. A. Neb.).

In re Sayed, 26 A. B. R. 444, 185 Fed. 962 (D. C. Mich.): "It is elementary to the definition of a forbidden preference, considered under any section and for any purpose, that it must have been made by the debtor 'while insolvent.' A solvent debtor cannot make a preference."

In re Veneer & Panel Co., 6 A. B. R. 271 (D. C. Wis., affirmed sub nom. McDonald v. Daskam, 8 A. B. R. 543, 116 Fed. 276): "It is true that the transaction on which the creation of a lien depends in each claim falls within the period of four months preceding the filing of the petition in bankruptcy; but it is equally true, under the testimony, that the corporation was solvent, within the definition of the act, up to the occurrence of the fire, on July 23rd. The inhibitions of § 60 apply only to preferences given when the debtor is insolvent in fact, and if a lien was perfected before the fire, in the case as presented, it is not affected by that section, although it may remain open to question under § 67, as to 'a present consideration.'"

Troy Wagon Wks. v. Vastbinder, 12 A. B. R. 352, 130 Fed. 232 (D. C. Pa.): "But it is essential to a preference that the debtor should have been insolvent at the time, and unless this appears there is no act of bankruptcy."

§ 1343. Definition of Insolvency under Present Act.—Insolvency, as the term is used in the present Bankruptcy Act, is different from what is usually meant in bankruptcy and insolvency law by the term. Its time-honored, legal meaning as used in insolvency proceedings, is inability of the debtor to meet his obligations as they mature in the usual course of business. And this was what was meant by the law of 1867.⁹⁸

Carson v. Chicago Title & Trust Co., 5 A. B. R. 824, 182 U. S. 438: "It is pointed out that insolvency has a different meaning under the Act of 1898 than it had under the Act of 1867. Under the latter, the debtor was insolvent when he was unable to pay his debts in the ordinary course of business. Under the former, when the aggregate of his property at a fair valuation is insufficient to pay his debts."

However, such a definition would make almost every merchant insolvent in the eyes of the law during seasons of panic and financial stringency such as occurred in the United States, for instance, during the dark days of 1893 and 1894, when the wealthiest and most prosperous business men were unable to pay their notes and bills as they became due. Money itself, the medium of payment, was hoarded. Banks had to resort to the artifice of clearing-house scrip—had to create a new kind of money in fact. It was next to impossible to raise money on the best collateral security, and real estate loans of so-called "gilt-edged" value went begging for takers. Almost every merchant was insolvent if the usual legal definition was the test, for everyone, almost, was unable to meet his obligations as they matured in the due course of business. The likelihood that such financial stringencies and industrial depressions are to be recurring and frequently recurring phenomena in the commercial world, undoubtedly was the reason that

⁹⁸ Hussey v. Dry Goods Co., 17 A. B. R. 513 (C. C. A. Kas.); Stevenson v. Milliken-Tomlinson, 13 A. B. R. 201 (Sup. Jud. Ct. Me.); Upson v. Mt.

Morris Bk., 14 A. B. R. 6 (N. Y. Sup. Ct. App. Div.); In re Andrews, 16 A. B. R. 390, 144 Fed. 922 (C. C. A. Mass.).

the framers of the present Bankruptcy Act, coming to their work only two or three years after the crisis of 1893, rejected as intolerable a definition of insolvency such as this, as a basis for bankruptcy proceedings. Indeed, this sweeping definition of insolvency was one of the causes of the popular hatred that grew up against the old Bankruptcy Law of 1867, and was one of the causes of the downfall of that law and of the reluctance of Congress to pass another Bankruptcy Act. Accordingly, Congress chose the more liberal definition and the definition most nearly approximating to the popular idea of insolvency that they set forth in § 1, clause 15, of the Statute, in the following words:

"A person shall be deemed insolvent within the provisions of this act whenever the aggregate of his property, exclusive of any property which he may have conveyed, transferred, concealed or removed, or permitted to be concealed or removed, with intent to defraud, hinder or delay his creditors, shall not at a fair valuation, be sufficient in amount to pay his debts."⁹⁹

Carson, etc., v. Chicago Title & Trust Co., 5 A. B. R. 824, 182 U. S. 438: "The other weakness in the argument is that it exaggerates the difference between the definitions of insolvency and overlooks an advantage to the creditor in the definition contained in the Act of 1898. Inability to pay debts in the ordinary course of business usually accompanies an insufficiency of assets. It may not, of course. At times a debtor's property, though amply sufficient in value to discharge all of his obligations, may not be convertible without sacrifice into that form by which payments may be made. The law regards that possibility. In this there is indulgence to the debtor, and through him to preferred creditors."

Martin v. Bigelow, 7 A. B. R. 220 (N. Y. Sup. Ct.): "To say of a man that he is in failing circumstances, or that he is unable to pay all his debts in full, which means presently unable so to do, is quite a different thing from alleging that his property, taken at a fair valuation, is not sufficient in amount to pay his debts."

And it is to be noted that the definition adopted in the present law is the same as that which for centuries has been the accepted meaning of the term insolvency as used in the law of fraudulent transfers. The term "insolvency," as understood in dealing with contracts and transfers challenged on the ground of fraud, actual or constructive, has always had reference to the insufficiency of the debtor's assets to cover his liabilities, although as understood in the administration of insolvent and former bankrupt laws, it has usually referred to the mere inability of the debtor to pay his debts as

⁹⁹. In *re Andrews*, 16 A. B. R. 390, 144 Fed. 922 (C. C. A. Mass.); *Hussey v. Dry Goods Co.*, 17 A. B. R. 513 (C. C. A. Kas.); In *re Rung Furn. Co.*, 10 A. B. R. 44 (Ref. N. Y.); *Stevenson v. Milliken-Tomlinson Co.*, 13 A. B. R. 206, 99 Me. 320; *Upson v. Mt. Morris Bk.*, 14 A. B. R. 6 (N. Y. Sup. Ct. App. Div.); In *re Crenshaw*, 19 A. B. R. 502, 156 Fed. 638 (D. C. Ala.);

Tumlin v. Bryan, 21 A. B. R. 319, 165 Fed. 166 (C. C. A. Ga.); *Harder v. Clark*, 23 A. B. R. 756 (City Court of New York); *Newman v. Dry Goods Co.*, 31 A. B. R. 399 (Kansas City Court of Appeals), quoted at §§ 1407 and 1277 note; *Hewitt v. Boston Strawboard Co.*, 31 A. B. R. 652 (Mass.).

they matured in the usual course of business.¹

Compare, *Grunsfeld v. Brownell*, 11 A. B. R. 601 (Sup. Ct. New Mex.): "The term insolvency as used in bankruptcy and insolvency laws means the inability of a person to pay his debts as they mature in the ordinary course of business, but as used in a general sense, it means a substantial excess of a person's liabilities over the fair cash value of his property."

It will be useful to explicate this definition in order to give a somewhat clearer idea of the meaning of bankruptcy insolvency.

§ 1344. Property Fraudulently Disposed of, Not to Be Counted as Assets.—Property fraudulently disposed of is not to be counted. In arriving at the property that is to be counted in making up the aggregate, all property conveyed, transferred, concealed or removed or permitted to be concealed or removed with intent to defraud or hinder creditors, is to be excluded.²

Thus it is possible that a debtor who has plenty of property to pay all he owes, may make himself insolvent within the bankruptcy definition by fraudulently transferring or concealing so much of it that that which is left will not be enough, even at a fair valuation, to pay all the debts. And so, under such circumstances, if the creditors succeed in recovering the property fraudulently disposed of, they may get their claims paid in full, notwithstanding the bankrupt himself could not say he was not insolvent without confessing to the frauds he himself had perpetrated. The transfer may itself create the insolvency.³

Thus it is possible that a man may be insolvent in bankruptcy under the present definition and yet his creditors ultimately get paid in full.⁴

But property which might be, but is not, claimed by third parties to be recoverable by them as having been transferred to the bankrupt in fraud of such third parties' rights, is not to be excluded.⁵

§ 1345. But Equity of Redemption Counted, if Fraudulent Conveyance by Way of Security.—If the fraudulent conveyance be by way

1. *Marvin v. Anderson*, 6 A. B. R. 520, 87 N. W. 226 (D. C. Wis.); compare, *In re Doscher*, 9 A. B. R. 547, 556, 120 Fed. 408 (D. C. N. Y.); also, see *Martin v. Bigelow*, 7 A. B. R. 218 (Sup. Ct. N. Y.), and *Lavor v. Seiter*, 5 A. B. R. 576 (N. Y. Sup. Ct.).

2. Bankr. Act, § 1 (15); *In re Baumann*, 3 A. B. R. 196, 96 Fed. 946 (D. C. Tenn.); *obiter*, *In re Doscher*, 9 A. B. R. 547, 556, 120 Fed. 408 (D. C. N. Y.); *In re Hines*, 16 A. B. R. 296, 144 Fed. 142 (D. C. Ore.); *inferentially*, *Acme Food Co. v. Meier*, 18 A. B. R. 550, 153 Fed. 74 (C. C. A. Mich.); *In re Crenshaw*, 19 A. B. R. 502, 156 Fed. 638 (D. C. Ala.); to same effect in fraudulent transfer

cases, *Phillips Tr. v. Kleinman*, 23 A. B. R. 266 (Pa. Com. Pleas); *Utah Ass'n of Credit Men v. Boyle Fur. Co.*, 26 A. B. R. 867 (Sup. Ct. Utah); *In re Duke & Son*, 28 A. B. R. 195, 199 Fed. 199 (D. C. Ga.).

3. *Phillips, trustee, v. Kleinman*, 23 A. B. R. 266 (Pa. Com. Pleas). Compare, *ante*, § 1218½.

4. *Instance*, *In re Shoesmith*, 13 A. B. R. 645, 135 Fed. 684 (C. C. A. Ills.): Admitting possession of assets at time of filing of petition but declaring they were subsequently "invested" without disclosing where or how kept meanwhile.

5. *In re Aschenbach Co.*, 23 A. B. R. 95, 174 Fed. 396 (C. C. A. N. Y.).

of mortgage or other security, the equity of redemption is, however, to be counted in.⁶

Acme Food Co. v. Meier, 18 A. B. R. 550, 153 Fed. 74 (C. C. A. Mich.): "Upon the issue that these conveyances were intended as preferences and, therefore, acts of bankruptcy under subdivision 2 of § 3 of the act it was admissible to show that these deeds were intended only as securities and the value of the equity of redemption at the date of each such conveyance. In *Lansing Boiler Works v. Ryerson*, cited above, we held that the interest of a mortgagor might be taken into account in determining whether when the mortgage was made insolvency existed so as to constitute the security a preference. * * * Thus construed, there was no error in directing the jury to estimate the value of the equity of redemption in determining solvency at the date of each such conveyance. We know of no authority which will justify the exclusion of equitable interests belonging to a debtor when we come to the question of his solvency or insolvency in a bankrupt proceeding."

§ 1346. Property Preferentially Conveyed as Security Not to Be Excluded.—Property not fraudulently but merely preferentially transferred as security, however, is not to be excluded, but is to be counted in as part of the assets.⁷

In *re Doscher*, 9 A. B. R. 547, 554, 120 Fed. 403 (D. C. N. Y.): "Where property is transferred in fraud of creditors, the statute contemplates that the bankrupt shall not have the benefit of its valuation in determining whether he is insolvent. Where property is transferred in payment of or as security for a just debt, the mere fact that it may involve a preference in bankruptcy, should bankruptcy proceedings be instituted, does not exclude it from consideration in determining the debtor's solvency."

§ 1347. Exempt Property Counted.—Exempt property is to be counted.⁸

Compare In *re Duke & Son*, 28 A. B. R. 195, 199 Fed. 199 (D. C. Ga.): "In fixing the assets in the foregoing statement I have counted the exempt property as an asset. I do this because it is unnecessary, under the facts, to determine whether such exempt property should or should not be counted. If it were necessary to determine this question of law, in my opinion, exempt property should not be counted."

6. *Lansing Boiler, etc., Wks. v. Ryerson & Son*, 11 A. B. R. 558, 128 Fed. 701 (C. C. A. Mich.).

7. *Lansing Boiler & Engine Wks. v. Ryerson & Son*, 11 A. B. R. 558, 128 Fed. 701 (C. C. A. Mich.); compare, impliedly, to same effect, In *re Norcross*, 1 A. B. R. 644 (Ref. Mo.); compare, analogously, as to counting in preferred creditors among liabilities, In *re Cain*, 2 A. B. R. 378 (Ref. Ills.); *McMurtrey v. Smith*, 15 A. B. R. 427, 142 Fed. 853 (Special Master Tex., affirmed by D. C.); *Acme Food Co. v. Meier*, 18 A. B. R. 550, 153 Fed. 74 (C. C. A. Mich.); *Utah Ass'n of Credit Men v. Boyle Fur. Co.*, 26 A. B. R. 867 (Sup. Ct. Utah).

"Preferred" Debt Distinguished from "Secured" Debt.—A "preferred" debt is to be distinguished from a "secured" debt, In *re Busby*, 10 A. B. R. 650, 124 Fed. 469 (D. C. Penn.).

8. In *re Hines*, 16 A. B. R. 295, 144 Fed. 142 (D. C. Ore.); In *re Crenshaw*, 19 A. B. R. 502, 156 Fed. 638 (D. C. Ala.); *Utah Ass'n of Credit Men v. Boyle Fur. Co.*, 26 A. B. R. 867 (Sup. Ct. Utah); *Louisiana, etc., Soc. v. Segen*, 28 A. B. R. 407, 196 Fed. 903 (D. C. La.). Contra, *Underleak v. Scott*, 28 A. B. R. 926 (Sup. Ct. Minn.). And compare, inferentially contra, *Gering v. Leyda*, 26 A. B. R. 137, 186 Fed. 110 (C. C. A. Neb.).

In *re Baumann*, 3 A. B. R. 196, 96 Fed. 946 (D. C. Tenn.): "It is entirely true, as stated by Mr. Justice Bradley, in *re Bass*, 3 Woods, 382, Fed. Cas. No. 1,091, 'that exempted property constitutes no part of the assets in bankruptcy, and that the assignee acquires no title to exempted property.' Nevertheless it does not follow that it is not to be counted when determining the question whether he be solvent or insolvent. * * * If Congress had intended to exclude from the terms of this definition property exempted by law from execution, the phrasing of the statute would have contained the exception either explicitly or by necessary implication—as if the statute had used the phrase 'the aggregate of his property subject to execution at law,' or 'the aggregate of his property available for the payment of his debts,' or 'the aggregate of his property, except such as is exempted by law;' and it is most natural that the language of the statute should have taken some such form if it had been the intention to exclude from the count the value of the exempted property. Although not leviable, it may be used voluntarily for the payment of these debts."

§ 1348. Partnership Not Insolvent, unless All Partners Insolvent.

—A partnership is not to be deemed insolvent unless the aggregate of all its own property, together with all of the individual property of its members in excess of their respective individual indebtedness, is less than its liabilities.⁹

Tumlin v. Bryan, 21 A. B. R. 319, 165 Fed. 166 (C. C. A. Ga.): "And besides, we find no evidence showing what property was owned by the individual members of the bankrupt firm in July, 1906. * * * As each member of the partnership is liable individually for the partnership debts, it seems to follow that, to show such insolvency as to entitle the trustee to recover, the insolvency of the members of the firm should be proved. If a condition exists whereby all diligent creditors may obtain payment in full, it seems useless and unjust to sustain a suit against a defendant who has only collected what was due to him. It is true that a partnership may be treated as an entity, separate from its individual members, for the purpose of its adjudication as a bankrupt * * * but, in a suit to recover a preference, it is not only the insolvency of an intangible entity, but the insolvency of its responsible component parts, that lies at the foundation of the right to relief. If the component parts of the firm may be made to pay the firm's debts, the suit lacks reason and substance, and it cannot be held that the defendant has obtained a greater percentage of his debt than other creditors of the same class. If the members of the firm are solvent, all creditors may be paid in full. If the individual members of the partnership are not shown to be insolvent at the date of the payments, the preference is not voidable."

Worrell v. Whitney, 24 A. B. R. 749, 179 Fed. 1014 (D. C. Pa.): "As I view the case, however, it must be decided on another proposition. As I have just said, the firm considered merely as an entity was insolvent on March 22, but there is almost no evidence concerning the financial situation of the partners as individuals as that time. It is impossible therefore to say that the indi-

9. See cases cited ante, chapter III, "Who May Be Thrown Involuntarily into Bankruptcy," division 3, subdiv. "B;" "Partnerships," § 60. *Crancer & Co. v. Wade*, 25 A. B. R. 880 (Sup. Ct. Okla.); *Francis v. McNeal*, 26 A. B. R. 555, 186 Fed. 481 (C. C. A. Pa.);

In *re Duke & Son*, 28 A. B. R. 195, 199 Fed. 199 (D. C. Ga.); *Washington Cotton Co. v. Morgan & Williams*, 27 A. B. R. 638, 192 Fed. 310 (C. C. A. Ga., affirming *In re Morgan & Williams*, 25 A. B. R. 861).

vidual assets of the partners taken in connection with the assets of the firm would not have been more than sufficient to pay all the firm debts. The only evidence on the subject of individual insolvency is to be found in the fact that on May 20, two months later, the petition was filed upon which both members were adjudged bankrupt both as individuals and as a firm. But this with-out more does not enable me to decide safely that they were insolvent as individuals on March 22. No effort was made to prove their individual insolvency at that time. One of the bankrupts was not examined at all, and the other was asked no questions concerning his individual condition when the conveyance was made. With proof upon this subject under the trustee's control, he can hardly expect the court to draw uncertain inferences concerning a fact that he might have established with at least reasonable certainty. The necessity for such proof is supported by * * * the bill is dismissed."

§ 1349. **Property to Be Taken at "Fair Valuation."**—Again, it must be noted that the property counted in must be counted in at a fair valuation.¹⁰

What constitutes fair valuation is difficult to define.¹¹ We can say, however, what it is not.

§ 1350. **"Fair Valuation," Not Value at Sacrifice Sale.**—It is not the valuation that would prevail at sheriff's sale, sacrifice sale or forced sale.

Thus, where the bankrupt is a going concern, the value of its assets after the levy of an execution and the consequent cessation of its business may not be the fair valuation.¹²

Nor may such valuation be what the assets actually brought at the sale by the trustee in bankruptcy.¹³

§ 1351. **Market Value, as "Fair Valuation."**—Moreover, even the market price probably would not be the fair valuation in all cases; for instance property that has no market value at all and property whose market value is abnormally low owing to extraordinary circumstances or financial depression. However, the market valuation of property would usually be its fair valuation except in the instances cited and similar ones.¹⁴

10. Bankr. Act, § 1 (15); *obiter*, *Brittain Dry Goods Co. v. Bertenshaw*, 11 A. B. R. 630, 68 Kas. 734. See also, cases cited in succeeding paragraphs herein; *Newman v. Dry Goods Co.*, 31 A. B. R. 399 (Kansas City Court of Appeals), quoted at §§ 1407 and 1277, note; *In re Duke*, 28 A. B. R. 195, 199 Fed. 199 (D. C. Ga.).

11. In determining the fair valuation in deciding whether an intent to prefer exists on the debtor's part so as to make the preference an act of bankruptcy, it would be permissible to show that the alleged bankrupt actually and bona fide thought a certain valuation would be a fair valuation that would make his assets appear to

be sufficient to cover his liabilities, whether in fact they were sufficient or not. See ante, "Intent to Prefer as an Element of Second Act of Bankruptcy," § 132.

Stipulation as to "Fair Valuation."—*Gering v. Leyda*, 26 A. B. R. 137, 186 Fed. 110 (C. C. A. Neb.).

12. *Chic. T. & T. Co. v. Roebbling's Sons*, 5 A. B. R. 368, 107 Fed. 71 (U. S. C. C. Ill.); compare, to same effect, *In re Rung Furn. Co.*, 10 A. B. R. 51 (Ref. N. Y.).

13. *Rutland Co. Nat. Bk. v. Graves*, 19 A. B. R. 446, 156 Fed. 168 (D. C. Vt.).

14. Price obtained by purchaser at private sale, on resale of the goods

Duncan v. Landis, 5 A. B. R. 649, 106 Fed. 839 (C. C. A. Pa.): "The words 'fair valuation' are equivalent to the present market value of the property in question, but such market value is not to be ascertained by what a purchaser would give who desires to take advantage of the necessities and embarrassments of the owner at a price less than its real value and a charge to the effect that such value should be fixed by the situation of the debtor the number and amount of the obligations owed by such debtor and the time when they were due, as elements to be regarded by the purchaser, is erroneous."

In *re Hines*, 16 A. B. R. 296, 144 Fed. 142 (D. C. Ore.): "As it respects property considered in a commercial sense, I can conceive of no better or surer standard by which to arrive at a fair valuation than the market value; that is, what the property will probably bring, or is worth in the general market, where everybody buys. It could not be what it is worth to one person or to another specially circumstanced, or having special use for a particular article, but what it is worth as a marketable commodity, at a given time, with no special conditions prevailing other than affect the market generally in the locality where the commodity is for sale."

Stern v. Paper, 25 A. B. R. 451, 183 Fed. 228 (D. C. N. D.): "'Fair valuation' means such a price as a capable and intelligent business man could presently obtain for the property after conferring with those accustomed to buy such property. Such a value will depend upon many circumstances, such as age and condition of the stock, the season of the year, and the state of trade."

§ 1352. **"Fair Valuation" Where Bankrupt "Going Concerns" Not "Scrap" nor "Wrecker's" Value.**—Where the bankrupt is a "going concern" at the date of the commission of the act of bankruptcy, that fact must be taken into account in fixing "fair valuation;" and "scrap" values or "wrecker's" values will not suffice.¹⁵

Paper Co. v. Goembel, 16 A. B. R. 28 (C. C. A. Ills.): "The valuation for the test of solvency or insolvency under the issue must relate to the conditions, as a going concern, when the alleged preference was given, and not to the mere dead matter after bankruptcy intervened."

But the failing condition of the debtor, though still a "going concern," may be taken into account as influencing the actual "fair valuation" of book accounts.

Spencer v. Nekemoto, 24 A. B. R. 517 (D. C. Hawaii): "Although it is hard to appraise such accounts, which must be considered in relation to a going concern, yet it is very evident that with the business on a decline, as his was in May—his creditors refusing further credit—that the book accounts would not be worth as much as if the business were in a prosperous condition."

shortly after the transfer, has been held incompetent, *Sebring v. Wellington*, 6 A. B. R. 671 (N. Y. Sup. Ct. App.). But see strong dissenting opinion.

The market value, the value which the bankrupt itself could have gotten for the assets, is the "fair" valuation,

so it is held in *In re Marine Iron Works*, 20 A. B. R. 390, 159 Fed. 753 (D. C. N. Y.).

15. Instance, *Motor Vehicle Co. v. Oak Leather Co.*, 15 A. B. R. 808 (C. C. A. Ills.); impliedly, *Chic. Title & T. Co. v. Roebbing's Sons*, 5 A. B. R. 371, 107 Fed. 71 (C. C. Ills.).

§ 1353. **"Fair Valuation" of Choses in Action and Intangible Property.**—The face value of choses in action is not to be taken if it is not the actual value.

Thus, the actual value of accounts must govern in determining the question of insolvency;¹⁶ likewise of insurance policies.¹⁷

Likewise, with the value of bonds, leases, patents, licenses and securities and of other intangible property, it is the actual, fair value that prevails.¹⁸

§ 1353¹/₂. **"Good Will" as an Asset.**—Doubtless "good will" is an asset which may be taken into account in arriving at "fair valuation;" indeed, such may often be the chief asset. However, its value is very difficult, ordinarily, to determine, and great abuse is likely to creep into an estimate of it.

Compare, *McElvain v. Hardesty*, 22 A. B. R. 320, 169 Fed. 31 (C. C. A. Mo.): "The trial court also allowed a recovery of the sum of \$600 for the good will of the business of C. & C., claimed to have been transferred to McElvain. Without expressing any opinion as to when and under what circumstances, if at all, the good will of a business may be 'property' within the meaning of § 60a and b of the Bankruptcy Act, we content ourselves by stating the conclusion reached that, if the saloon ever had any good will of value known to the law, it had been utterly destroyed by the methods pursued and the results achieved by the bankrupts and McElvain during the seven months of their relationship to it. The evidence satisfies us that there was no good will of value at the time of the transfer, and that the allowance of anything in favor of the trustee on that account was erroneous."

§ 1354. **Admissions of Insolvency by Bankrupt Not Competent against Creditor.**—Proof of admissions of insolvency itself, or of admissions of facts tending to show insolvency, made by the bankrupt, even before bankruptcy, are not competent evidence against the preferred cred-

16. In *re Coddington*, 9 A. B. R. 243, 118 Fed. 281 (D. C. Penn.); *Benjamin v. Chandler*, 15 A. B. R. 440 (D. C. Penn.); impliedly, *Spencer v. Neke-moto*, 24 A. B. R. 517 (D. C. Hawaii), quoted at § 1352.

"**Dead Accounts.**"—Instance, *Alexander v. Redmond*, 24 A. B. R. 620, 180 Fed. 92 (C. C. A. N. Y.): It has been held, indeed, that outstanding accounts, in favor of the bankrupt must be such as could be realized upon under an execution in order to warrant consideration as assets. *Louisiana & Soc. v. Segen*, 28 A. B. R. 19, 407, 196 Fed. 903 (D. C. La.). But such a rule is too strict. "Fair valuation" would imply a more liberal rule, for oftentimes accounts are good as a practical matter that would not be collectible by legal process."

17. *Bogen & Trummell v. Protter*, 12 A. B. R. 288, 129 Fed. 533 (C. C. A. Ohio); *Benjamin v. Chandler*, 15 A. B. R. 440 (D. C. Penn.).

18. Instance, *First Nat'l Bk. v. Ice*

Co., 14 A. B. R. 448, 136 Fed. 466 (D. C. Penn.): Disputed liability of bondholders on bonus stock issued to them not counted in as assets.

Instance, *McGowan v. Knittel*, 15 A. B. R. 1, 137 Fed. 1015 (C. C. A. Penn., reversing *Knittel v. McGowan*, 14 A. B. R. 209, 137 Fed. 453): Record of a reopened judgment against the bankrupt should not be admitted before the jury; especially where opened generally and not specially to let in some particular defense.

Troy Wagon Wks. v. Vastbinder, 12 A. B. R. 352, 130 Fed. 232 (D. C. Penn.): Leases and securities, face value \$4,000.00 conceded actual value \$1,000.00.

Instance, *Motor Vehicle Co. v. Oak Leather Co.*, 15 A. B. R. 808 (C. C. A. Ills.): Patent.

Instance, *In re Foley*, 15 A. B. R. 832 (Ref. Pa.): Liquor license: Claimed to be worth \$10,000.00 but testimony that only made \$100.00 in 18 months.

itor on a suit for recovery of the preference.¹⁹

The bankrupt's uncorroborated testimony as to the precise time of becoming insolvent has been held not sufficient to establish the fact.²⁰

§ 1355. Bankrupt's Books Admissible.—Books of the bankrupt, when properly qualified as evidence, are competent evidence on the question of his insolvency.²¹

Of course their competency is not on the basis of their being admissions, but rather of their being contemporaneous memoranda; except where the issue is the commission of an act of bankruptcy and not the recovery of a preference.

§ 1356. Schedules Inadmissible against Preferred Creditor.—The schedules filed by the bankrupt are inadmissible against the alleged preferred creditor to prove the bankrupt's insolvency. They are the admissions of a mere assignor after he has parted with his interest to the alleged preferred creditor.²²

§ 1357. Inventory and Appraisement in Bankruptcy, whether Admissible.—It has been held that the inventory and appraisement taken by the bankruptcy court are competent evidence.²³

But it is difficult to see how the preferred creditor can be thus bound. Of course, the testimony of the appraisers would likely be admissible, if qualified as witnesses, as throwing light upon the financial condition of the bankrupt at the time of the alleged preferential transfer; but the theory on which the appraisal itself, even though official, is admissible, is not plain.²⁴

§ 1358. Whether Sale by Receiver in State Court or by Trustee in Bankruptcy, Competent.—Prices obtained by a receiver in the State Court before the bankruptcy, although somewhat subsequently to the transfer complained of, are admissible in proof of the fair value at the time of the transfer, in the absence of better proof, and the exclusion of such prices from evidence has been held reversible error.²⁵ Where the evidence

19. But of course are perfectly competent against the bankrupt on a petition for his adjudication as bankrupt. In re Lange, 3 A. B. R. 231, 97 Fed. 197 (D. C. N. Y.).

20. In re Linton, 7 A. B. R. 676 (Ref. Penn.).

Uncorroborated testimony of bankrupt as to his insolvency; the testimony of the bankrupt as to his insolvency is not to be rejected because uncorroborated. Collett v. Bronx Nat'l Bk., 29 A. B. R. 454, 200 Fed. 111 (D. C. N. Y.).

21. In re Coddington (Docker-Foster Co.), 10 A. B. R. 584, 123 Fed. 190 (D. C. Penn.); obiter, Hackney v. Hargreaves Bros., 13 A. B. R. 164, 68 Neb. 634.

22. Hackney v. Raymond Bros. Clark Co., 10 A. B. R. 213 (Sup. Ct.

Neb., reversed in 13 A. B. R. 164, Sup. Ct. Neb.); compare, same rule as to alleged fraudulent conveyances, Halbert v. Pranke, 11 A. B. R. 620, 91 Minn. 204; contra, Hackney v. Hargreaves, 13 A. B. R. 164, 68 Neb. 634; contra. In re Docker-Foster Co., 10 A. B. R. 584, 123 Fed. 190 (D. C. Pa.).

23. Hackney v. Hargreaves Bros. and v. Raymond Bros. Clark Co., 13 A. B. R. 164, 68 Neb. 634; In re Docker-Foster Co., 10 A. B. R. 584, 123 Fed. 190 (D. C. Penn.); compare, In re Soudans Mfg. Co., 8 A. B. R. 59, 113 Fed. 804 (C. C. A. Ind.).

24. Compare, In re Soudans Mfg. Co., 8 A. B. R. 50, 113 Fed. 804 (C. C. A. Ind.).

25. In re Block, 6 A. B. R. 300, 109 Fed. 790 (C. C. A. N. Y.).

shows that the value of the assets has not varied from the time of the alleged preference to the date of a sale by the trustee in bankruptcy, the sale price has been held competent evidence on the issue of insolvency.²⁶ It has also been held that the referee's order confirming the report of the sale is also competent, but not conclusive.²⁷ This ruling, however, though perhaps justifiable in the absence of better evidence, is treading on dangerous ground.^{27a}

§ 1359. Referee's Allowance of Claims, Whether Admissible.—

And it has been held that the orders of allowance of claims by the referee are not admissible, as to the amount of the bankrupt's indebtedness, as against an alleged preferred creditor.²⁸

Cullinane v. State Bk., 12 A. B. R. 776, 123 Iowa 340: "To prove the amount of indebtedness of the firm, the plaintiff called as a witness the referee in bankruptcy, and he was permitted to testify in respect of the number and amount of claims filed with and allowed by him. This testimony was objected to by defendant as incompetent, in that defendant was in no sense a party to the bankruptcy proceedings, and was not bound thereby, or by any findings made therein. We think that under the issues as presented by the pleadings the objection should have been sustained. The defendant was relying upon its mortgage as a specific lien upon the property covered thereby, and under the Bankrupt Act it could be divested of that lien only upon proof of actual insolvency. The finding of the bankruptcy court upon that question, or of any fact involved therein, was not *res adjudicata* as against defendant, inasmuch as it was not in any sense a party to the bankruptcy proceedings."

But (at any rate, wherever the alleged preferred creditor is applying to the bankruptcy court for dividends) it would seem that he is bound, as a party, by the referee's adjudication as to the validity of claims. This involves quite a different principle from that of the admissibility of the proofs of debt filed by the various creditors.²⁹

§ 1360. Admissions of Agent, as to Insolvency of Principal.—The admissions of an agent are not competent on the subject of insolvency unless within the scope of his authority; thus the admissions of the husband of the bankrupt, acting as the bankrupt's manager in the conducting of her business, have been held not competent to prove insolvency.³⁰

26. *Bank v. Sundheim*, 16 A. B. R. 866, 145 Fed. 795 (C. C. A. Penn.); *Morris v. Tannebaum*, 26 A. B. R. 368 (Ref. N. Y.).

27. *Bank v. Sundheim*, 16 A. B. R. 866, 145 Fed. 795 (C. C. A. Penn.).

27a. See discussion in preceding paragraph, § 1357.

28. Apparently *contra*, *Credit Men v. Furniture Co.*, 26 A. B. R. 867 (Utah), but in this case it appears that the "allowance" was not made by the referee, who is, by the bankruptcy

act, "The court of bankruptcy," but was made by the trustee—an anomalous proceedings. Of course, the trustee has no power to make an order of allowance and certainly such an "allowance" could hardly attain the dignity of a judicial determination.

29. Compare, *Jacobs v. United States*, 20 A. B. R. 550, 161 Fed. 694 (C. C. A. Mass.), quoted at § 2329½.

30. *Duncan v. Landis*, 5 A. B. R. 675, 106 Fed. 839 (C. C. A. Penn.).

§ 1360½. Bankrupt's General Examination, Whether Admissible.

—It has been held that the general examination of the bankrupt may be admitted in the proof of indebtedness as against the preferential transferee.³¹

Of course, the bankrupt is a competent witness on the subject of his debts and liabilities but his previous examination could be admissible in a controversy between the trustee and a transferee only on the theory that it was a deposition already taken in the case, which we find is an incorrect theory.³²

§ 1361. Return of Execution Unsatisfied, Whether Prima Facie Proof of Insolvency.—It has been held, that the return of an execution unsatisfied in whole or in part is not prima facie proof of insolvency.³³

§ 1362. Adjudication of Bankruptcy as Res Adjudicata on Question of Insolvency.—The adjudication of bankruptcy is held by some cases to be conclusively binding upon all creditors in subsequent actions between them and the trustee as to all points necessarily decided therein; from which it would follow that, where insolvency is a necessary element of the act of bankruptcy on which the adjudication is based, the adjudication itself will be res adjudicata as to insolvency at the time of the commission of the act.³⁴

Lazarus v. Eagan, 30 A. B. R. 287, 206 Fed. 518 (D. C. Pa.): "The decree of this court put in evidence adjudicating on the 28th of December, 1911, W. J. Greggs, a bankrupt, conclusively established the fact at issue, as alleged in the petition, that Greggs was insolvent when he transferred his property to his wife and afterwards to Eagan. Any other holding would lead to endless confusion in the administration of the law, and would in many cases, nullify one of the principal purposes of the Bankruptcy Act, as was said in *De Groff v. Sang*, 92 App. Div. (N. Y.) 564; S. C., 87 N. Y. 78. And it matters not that Eagan was actually without notice of these proceedings. An adjudication being an adjudication in rem, all persons interested in the res are regarded as parties to the bankruptcy proceedings. Among such parties are not only the trustee but all creditors, including lienors."

But the better reasoning seems to be that the doctrine of res judicata does not apply in such cases, for the reasons that the subject matter and the relief in the two cases are not the same. In the first case the status of the debtor is the subject matter, and upon that matter the adjudication of bankruptcy is binding upon the whole world, being an adjudication in

31. *Collett v. Bronx Nat. Bk.*, 29 A. B. R. 454, 200 Fed. 111 (D. C. N. Y.).

32. See post, § 1555.

33. *Levor v. Seiter*, 5 A. B. R. 576, 34 Misc. (N. Y.) 382; *In re Rung Furn. Co.*, 10 A. B. R. 51 (Ref. N. Y.).

34. See post, "Actions by Trustees," §§ 1774, 1776 and 1777; and ante, "Effect of Adjudication on Rights of

Parties," § 444, et seq. *Whitwell, Trustee v. Wright*, 23 A. B. R. 747 (N. Y. Sup. Ct. App. Div.), but this case is not to be commended for its reasoning; *Cook v. Robinson*, 28 A. B. R. 182, 194 Fed. 753 (C. C. A. Alaska); *Breckons v. Snyder*, 15 A. B. R. 112, 211 Penn. St. 176; *In re Virginia Hardwood Mfg. Co.*, 15 A. B. R. 137, 139 Fed. 209 (D. C. Ark.).

a proceedings in rem; but in the latter case the subject matter is the property, and though it may also be a proceedings in rem, the res is different.^{34a} At any rate, an adjudication on the ground of preference is not res judicata on the issue of the existence of a "reasonable cause for belief."^{34b}

§ 1363. **Ordinary Rules Apply in Proof of Insolvency.**—And, in general, the ordinary rules of evidence are to govern in the proof of insolvency.³⁵

§ 1364. **Date of Insolvency and "Fair Valuation," Date Immediately Preceding Transfer.**—The proof must show the "fair valuation" and insolvency at the time of the transfer, before the transfer (except, where, under the Amendment of 1910, the date of recording may be taken, at the trustee's option); and not the valuation nor insolvency created by the transfer itself.³⁶

In re Hines, 16 A. B. R. 297 (D. C. Ore.): " * * * the intendment being that the insolvency must exist at the time of suffering the preference to be taken; for, if the debtor is solvent, it would be perfectly proper and legitimate for him to make any sort of preference that he might see fit. The fact of suffering the preference, therefore, unless it might be under circumstances indicating that he intended to hinder, delay, or defraud certain of his creditors, could not be

34a. *Silvey & Co. v. Tifft*, 16 A. B. R. 12, 123 Ga. 804. Compare, *Levor v. Seiter*, 5 A. B. R. 576, 69 N. Y. Supp. 987 (reversed on other grounds 8 A. B. R. 459, 74 N. Y. Supp. 499).

34b. *Hussey v. Dry Goods Co.*, 17 A. B. R. 516, 148 Fed. 598 (C. C. A. Kans.), quoted at § 446.

35. Instance of Proof of Insolvency:
1. Corporation put into the hands of a receiver by its own directors on the ground of insufficiency of assets, yet a schedule accompanying it showing excess of assets; also investigation shows surplus. The mere admission of insufficiency of assets not enough where rebutted by proof. In re Doscher, 9 A. B. R. 547, 120 Fed. 408 (D. C. N. Y.).

2. Inability to pay debts at a later time, suspension of business, negotiations with creditors for composition, etc., are admissible as evidence tending to prove insufficiency of assets, in the absence of other evidence. In re Elmira Steel Co., 5 A. B. R. 488, 109 Fed. 456 (Special Master N. Y.).

But compare, *Martin v. Bigelow*, 7 A. B. R. 220 (Sup. Ct. N. Y.), where the adjudication of the debtor on March 11 was held not to relate back to establish his insolvency in the preceding November.

3. Offer of settlement made to creditors prior to bankruptcy on the basis of thirty cents on the dollar is evi-

dence not to be overcome by mere estimates of the value of a lease, good will and fixtures. In re Lange, 3 A. B. R. 231, 97 Fed. 197 (D. C. N. Y.). It is to be borne in mind, however, that this case arose on proof of an act of bankruptcy and might be affected by the possible incompetency of admissions of the bankrupt as against a preferred creditor himself in a suit for recovery of the preference.

4. Instance, In re Rodgers Milling Co., 4 A. B. R. 540, 102 Fed. 687 (D. C. Ark.).

5. Instances of insolvency not proved: *Hastings v. Fithian*, 13 A. B. R. 676 (Court Errors and Appeals N. J.); In re Chappell, 7 A. B. R. 608, 113 Fed. 545 (D. C. Va.).

6. Insolvency at the time of sale under attachment held to be sufficient proof of insolvency at the time of levying attachment, there being no substantial change intervening; In re Crafts-Riordan Shoe Co., 26 A. B. R. 449, 185 Fed. 931 (D. C. Mass.).

Value of neighboring property as proof of value of bankrupt's real estate. Compare, In re Carlile, 29 A. B. R. 372, 199 Fed. 612 (D. C. N. C.).

36. *Upton v. Mt. Morris Bk.*, 14 A. B. R. 11 (N. Y. Sup. Ct. App. Div.); *Chicago Title & Trust Co. v. Roebeling's Sons*, 5 A. B. R. 368, 107 Fed. 71 (D. C. Ills.).

permitted to affect the value of his assets. If such were the case, then a person, who was before perfectly solvent, might be rendered insolvent by an action, accompanied by an attachment, and his insolvency would depend upon whether he could pay his debts under the stress of the occasion, and not, under the simple inquiry prescribed by the Bankruptcy Act, whether the aggregate of his property, at a fair valuation, is sufficient in amount to pay his debts."

And fractions of a day may be taken into account.³⁷

§ 1364½. Date, Where Recording Necessary.—Where the transfer is made by means of an instrument which the State law requires to be recorded in order that it may be effective against levying creditors, the date at which the insolvency may be proved to have existed is the date of such recording, for not until recording is there an effective transfer, as against other creditors, under State law.

[Even before Amendment of 1910.] *McElvain v. Hardesty*, 22 A. B. R. 320, 169 Fed. 31 (C. C. A. Mo.): "The effect of the transfer to McElvain is to be judged as if made on the 7th day of July, 1905, when it was filed for record. If C. & C. were then insolvent, and if the effect of the enforcement of the transfer was to enable McElvain to obtain a greater percentage of his debt than any other of their simple contract creditors, the transfer constituted a preference within the meaning of the bankruptcy law. * * * As, for the purposes of this case, the transfer is to be treated as made on the date the agreement was recorded, so the transferee's belief or cause for belief concerning it must relate to that time."

Amendment of 1910.—The Amendment of 1910 to § 60 (b), expressly brings down to the date of transfer, or, to the date of recording where recording is "required," the proof of the insolvency.³⁸

§ 1365. Debts Owning but Not Yet Due Included in Bankrupt's Liabilities.—It is doubtless true that debts owing, although not yet due, are to be included among the bankrupt's liabilities in determining his insolvency.

§ 1366. Whether Contingent Liabilities Counted in Determining Insolvency.—It does not appear to have been finally settled, however, whether contingent liabilities, as distinguished from debts owing but not yet due, are to be included in the computation.³⁹

§ 1366½. Bankrupt as Surety or Guarantor, Debt to Be Counted.—Where the bankrupt is a surety or guarantor, the obligation is to be counted as a liability; and such has been the holding even where the guaranty is oral, the fact that it is not in writing affecting merely the proof, not the validity.

³⁷. *Upson v. Mt. Morris Bk.*, 14 A. B. R. 11 (N. Y. Sup. Ct. App. Div.).

³⁸. See Bankruptcy Act, § 60 (b), as amended in 1910.

³⁹. That they are not to be so included, see *obiter*, *In re Nassau*, 15 A. B. R. 303, 140 Fed. 912 (Ref. Penn.).

Fact of contingency of debts is to be taken into account in determining the intent of the bankrupt, no doubt. See *inferentially*, *Merchants' Nat. Bk. v. Cole*, 18 A. B. R. 44, 149 Fed. 708 (C. C. A. Ohio).

Huttig Mfg. Co. v. Edwards, 20 A. B. R. 349, 160 Fed. 619 (C. C. A. Iowa): "A surety or indorser for a bankrupt has been held to be a creditor within the meaning of the bankruptcy law * * * and upon the same principle a guarantor liable upon a fixed liquidated demand as this was, is a debtor to him who holds it, and his liability is to be counted in determining his financial status. That the guaranty may have been oral and therefore within the statute of frauds of Iowa where the transaction occurred is immaterial. The Iowa statute relates merely to the evidence or proof of the undertaking, and not to its validity."

§ 1367. Seventh Element of a Preference—Transfer or Recording within Four Months before Filing of Petition.—The transfer or other appropriation of property, or, when the transfer is such that the law requires the recording of it to make it effective [against creditors] then the recording of the transfer, must have been made within four months before the filing of the bankruptcy petition.⁴⁰

§ 1368. Preferences Obtained before Four Months, Not Voidable.—Preferences obtained before the four months period will not be disturbed⁴¹ except in one instance, namely, that mentioned in the last clause of § 60 (a):

"Where the preference consists in a transfer such period of four months shall not expire until four months after the date of the recording or registering of the transfer, if by law such recording or registering is required."

In *re Dunavant*, 3 A. B. R. 41, 96 Fed. 542 (D. C. N. Car.): "A proceeding in bankruptcy does not affect liens accruing more than four months before bankruptcy."

§ 1369. Nature of Limitation.—The four months limitation before the Amendment of 1903^{41a} was evidently by way of a statute of limitations. In theory and in fact before the Amendment of 1903, a preference existed whenever a payment was made out of an insolvent estate whereby one creditor got more than his share of the trust fund, no matter how long beforehand it was that the payment was made, the four months limitation being merely a statute of limitations for recovery, beyond which the court would not investigate transactions.⁴²

40. Bankr. Act, § 60 (a). Merely that a transfer occurred within the four months raises no presumption of a voidable preference, *Stich v. Beriman*, 15 A. B. R. 466, 49 N. Y. Misc. 104 (N. Y. Sup. Ct. App. Div.); *Tumlin v. Bryan*, 21 A. B. R. 319, 165 Fed. 166 (C. C. A. Ga.), quoted at § 1277, note; *Allen v. Gray*, 21 A. B. R. 828 (N. Y. Sup. Ct.); In *re Starkweather & Albert*, 30 A. B. R. 743, 206 Fed. 797 (D. C. Mo.); *Newman v. Dry Goods Co.*, 31 A. B. R. 399 (Kansas City Court of Appeals), quoted at § 1407 and § 1277, note.

41. In *re Girard Glazed Kid Co.*, 12 A. B. R. 295, 129 Fed. 841 (D. C.

Penn.); *Manning v. Patterson*, 19 A. B. R. 224, 156 Fed. 111 (D. C. N. J.); *Allen v. Gray*, 21 A. B. R. 828 (N. Y. Sup. Ct.); *Brown v. City National Bank*, 26 A. B. R. 638 (Sup. Ct. N. Y.); *Jackson v. Sedgwick*, 26 A. B. R. 836, 189 Fed. 508 (C. C. N. Y.); *Fitch v. Bank of Grand Rapids*, 26 A. B. R. 879 (Sup. Ct. Wis.); *Sturdivant Bank v. Schade*, 27 A. B. R. 673, 195 Fed. 188 (C. C. A. Mo.), reversing 26 A. B. R. 916; *First Nat. Bank v. Lanz*, 29 A. B. R. 247, 202 Fed. 117 (C. C. A. La.).

41a. Found only in § 60 (b), not in § 60 (a).

42. Before the Amendment of 1903

But since the Amendment of 1903 inserted into the very definition of a preference itself that it must have been a transfer or judgment within the four months period, and that such four months should not begin to run until the date of the filing or recording of the instrument creating the preference, where such filing or recording is required by the State statute to impart notice, it might have seemed that the four months' qualification was no longer by way of a statute of limitations, but an essential element of a preference itself; that is to say, after the Amendment of 1903, it was not merely that only preferences received within the four months were voidable but that a transaction was not even a preference unless occurring within the four months period.⁴³ And it would also seem to have followed as a corollary that the fact that the instrument was not recorded until within the four months would have operated *propria vigore* to bring the entire transaction within the four months period.

§ 1370. Agreements for Liens or for Other Transfers Not Effective until within Four Months, Voidable.—Agreements for liens or for other transfers,⁴⁴ made before the four months period, or at the time of the passing of the original consideration, but not effective until within the four months period, are voidable as preferences, if the other elements of a preference co-exist.

Thus, agreements at the time of making a loan or sale, to give a mortgage later, not executed until within the four months period, are voidable.⁴⁵

changed the law so that so-called "innocently" received preferences no longer needed to be surrendered as a prerequisite to the proof of claims, it was held in several cases that as to "innocently" received preferences, there was no time limit, *In re Abraham Steers Lumber Co.*, 7 A. B. R. 332 (C. C. A. N. Y., affirming 6 A. B. R. 315); *In re Jones*, 4 A. B. R. 563 (D. C. Mass.).

But in other cases it was held that, there being no express time limit fixed by the statute, the time limit expressly fixed as to preferences knowingly received would be adopted as an equitable rule, *In re Beswick*, 7 A. B. R. 395 (Ref. Ohio); *In re Dickinson*, 7 A. B. R. 679 (Ref. N. Y.).

43. But compare, *Loeser v. Bank & Trust Co.*, 17 A. B. R. 630 (C. C. A. Ohio, reversing *In re Chadwick*, 15 A. B. R. 528, 148 Fed. 975): "It must also be conceded that prior to the amendment of the bankrupt law by the amending Act of February 5, 1903, the preference, if free from actual fraud, would relate to the date of the making and delivery of the instrument creating it." Compare the reasoning in *In re Gallagher*, 6 A. B. R. 255 (Ref. Mass.). Compare, the reasoning in *Tatman v. Humphrey*, 12 A.

B. R. 62, 184 Mass. 361. Also compare, the reasoning in *In re Klingman*, 4 A. B. R. 254, 101 Fed. 691 (D. C. Iowa). Also compare, for history of the legislation, *In re Hunt*, 14 A. B. R. 416, 137 Fed. 694 (D. C. N. Y.). See post, § 1379, "Preferences as Affected by Recording."

44. "Equitable assignment," found to be merely a promise to pay a debt when in receipt of certain expected funds, *Speckman v. Smedley*, 18 A. B. R. 717, 153 Fed. 771 (D. C. A. Pa., affirmed in 19 A. B. R. 694, sub nom. *Smedley v. Speckman*).

45. *Pollock v. Jones*, 10 A. B. R. 616, 124 Fed. 166 (C. C. A. S. Car., affirming 9 A. B. R. 262); *In re Ronk*, 7 A. B. R. 31, 111 Fed. 154 (D. C. Ind.); *In re Dismal Swamp Contracting Co.*, 14 A. B. R. 175, 135 Fed. 415 (D. C. Va.); *Morgan v. Nat'l Bk.*, 16 A. B. R. 645, 149 Fed. 466 (C. C. A. W. Va.). See ante, § 1281. The following are apparently contra, under the law of 1867; *In re Jackson*, 15 N. B. Reg. 438; *Burdock v. Jackson*, 15 N. B. Reg. 318; *Douglass v. Voegeler*, 12 N. B. Reg. 493, Fed. Cas. 5271; *In re White*, 22 A. B. R. 200 (Ref. R. I.). Apparently contra, [1867] *In re Jackson*, 15 Nat. Bankr. Reg. 431; apparently con-

Lathrop Bank v. Holland, 30 A. B. R. 62 (C. C. A. Mo.): "The agreement that he would not dispose of the horses to be purchased, without its consent, and would give it a chattel mortgage at the end of the venture gave rise to a personal obligation, not a lien as against creditors. * * * If the bank had taken mortgages as the purchases were made but had refrained from recording them, it could not have prevailed against the trustee in bankruptcy. The oral agreement for a mortgage can give no greater right. The equity claimed by the bank is not different from that of any ordinary creditor who relies on his debtor's promise to do or not to do certain things in the future and refrains from adopting one of the various methods of protecting it. A purpose of the Bankruptcy Act and of State recording statutes is to discourage secret equities. We can conceive of a series of acts so secutively related as to be regarded as parts of one entire transaction, and, in contemplation of law, as having been done contemporaneously and therefore secure from disruption to the prejudice of the parties by intervening bankruptcy proceedings. But this case is not of that character."

In re Herman, 31 A. B. R. 243, 207 Fed. 594 (D. C. Iowa): "That it was made pursuant to an agreement to make the same, when the loans were made does not relieve it from operating as a preference, if the other essentials of a voidable preference are present."

In re Great Western Mfg. Co., 18 A. B. R. 263, 153 Fed. 123 (C. C. A. Neb.): "An agreement to mortgage or to transfer is not a mortgage or a transfer. The title remains in the owner unincumbered by the mortgage until the mortgage or transfer is effected. When the agreement is made before, and the mortgage or transfer within the four months, the title stands unincumbered by the latter at the commencement of the four months, and the proceeds of that title are pledged under the bankruptcy law for the benefit of all the creditors pro rata. Any subsequent mortgage or transfer withdraws that title or a portion of its value from these creditors, and a just and fair interpretation and execution of the act demands that such a mortgage or transfer should be adjudged voidable if it is otherwise so, and that the mortgagee or transferee should be remitted to his original agreement. In this way the property at the commencement of the four months and its value may be preserved for the general creditors, and the mortgagee or transferee may retain every lawful advantage his earlier contract confers upon him. Any other course of decision opens a new and enticing way to secure preferences, nullifies every provision of the law to prevent them and invites fraud and perjury. Hold that transfers within four months in performance of agreements to make them before that time do not constitute voidable preferences, and honest debtors would agree with their favored creditors before the four months that they would subsequently secure them by mortgages or transfers of their property, and just before the petitions in bankruptcy were filed they would perform their agreements. Dishonest men

tra, [1867] *Burdock v. Jackson*, 15 Nat. Bankr. Reg. 318; apparently *contra*, [1867] *Douglass v. Vogeler*, 12 Nat. Bankr. Reg. 493, Fed. Cas. No. 5271; *Roy v. Salisbury*, 27 A. B. R. 892 (N. Y. Sup. Ct.).

Under the law of 1867, on the basis that the assignee in bankruptcy stood in the bankrupt's shoes, and that equity would consider that done which was intended to have been done, it was

held that an agreement to execute a chattel mortgage not executed at the time of the original consideration but executed within the four months period, if not purposely withheld from execution, was valid. *In re Jackson*, 15 N. B. Reg. 438; *Burdock v. Jackson*, 15 N. B. Reg. 318; *Douglass v. Vogeler*, 12 N. B. Reg. 493, Fed. Cas. No. 5271.

who made no such contracts might falsely testify that they had done so and thus by fraud and perjury sustain preferential transfers and mortgages made within the four months to relatives or friends. The great body of the creditors would be left without share in the property of their debtor and without remedy, and a law conceived and enacted to secure a fair and equal distribution of the property of debtors among their creditors would fail to accomplish one of its chief objects. This court will hesitate long before it approves a rule so fatal to the most salutary provisions of the bankruptcy law, and our conclusion is:

"A mortgage or transfer of his property by an insolvent debtor within four months of the filing of a petition in bankruptcy against him, which otherwise constitutes a voidable preference, is not deprived of that character or made valid by the fact that it was executed in performance of a contract to do so, made more than four months before the filing of the petition."

Forbes v. Howe, 3 A. B. R. 475, 102 Mass. 427: "A mortgage given by an insolvent debtor to secure advances previously made is not purged of its character as an unlawful preference because it was given in pursuance of an agreement on which the advances had been made; nor because the debtor was induced to give it by the hope of obtaining further credit or means for the continuance of his business; nor because it was intended to make up security which had been reduced by the sale, with the consent of the mortgagee, of property included in a previous mortgage to him, under an understanding that new security should be given."

In re Smith (preference as act of bankruptcy) 23 A. B. R. 864, 176 Fed. 426 (D. C. N. Y.): "So, if the giving of the mortgage or deed was within the four months and the effect will be as stated in § 60, and the one receiving it had reasonable cause to believe a preference was intended, the fact that it was executed and delivered within the four months in execution of a prior oral agreement to execute it does not change the result or prevent the transfer being held a preference."

Obiter and merely inferentially, *Page v. Rogers*, 21 A. B. R. 496, 211 U. S. 575: "It is further said that I. B. Merriam agreed in writing, on November 15, 1902, to convey the coal lands to Thomas Merriam in satisfaction of the debts due to him or for which he was liable. It is, therefore, argued that, as the conveyance, on June 1, 1903, was in performance of this agreement, which antedated the bankruptcy proceedings by more than four months, it cannot be regarded as a preference. The facts, however, do not raise the question which was argued. Upon a proper interpretation of the evidence we need not determine whether an insolvent debtor may make an agreement to convey a substantial portion of his assets to a favored creditor, keep that agreement secret for more than four months, and then execute it in fraud of the rights of his other creditors, in favor of a creditor who then has reasonable cause to believe that he is receiving a preference. * * * The trust deed was not delivered unconditionally, and the parties to it intended that it should go into effect as a lien only when it was registered, which was never done. The instrument, though actually written, was never delivered as a present, valid, and subsisting obligation. It was executed and held in the possession of the grantor, to be delivered and to become operative as a conveyance at some future time, which never arrived. It was written and held ready for instant use, but never actually used until brought forward to excuse a payment which otherwise would be an unlawful preference. In other words, the paper was not as much as an unrecorded deed; it was not a deed at all."

Thus, agreements for repayment out of a particular fund not consummated until within the four months are voidable.⁴⁶

Smedley v. Speckman, 19 A. B. R. 694, 157 Fed. 815 (C. C. A. Pa.): "This testimony falls far short of evidencing the absolute appropriation by the assignor of the fund sought to be assigned, which is a fundamental requisite of a valid assignment, nor is there any evidence of that surrender by the assignor of all control over the fund that the law requires. A mere promise, though of the clearest and most solemn kind, to pay a debt out of a particular fund, is not an assignment of the fund, even in equity. To make an equitable assignment, there should be such an actual or constructive appropriation of the subject-matter as to confer a complete and present right in the party meant to be provided for, even where the circumstances do not admit of its immediate exercise. If the holder of the fund retain control over it, it is fatal to the claim of the assignee. 'The transfer must be of such a character, that the fund holder can safely pay, and is compellable to do so, though forbidden by the assignor.' *Christmas v. Russell*, 14 Wall. 69, 20 L. Ed. 762."

Torrance v. Winfield Nat'l Bk., 11 A. B. R. 185 (Kas.): "An agreement made, while negotiating for a loan, to make repayment out of a certain fund, or the proceeds of a particular enterprise, does not create a lien upon the fund or the proceeds of the enterprise, and, where repayment is made out of the designated

46. Compare, *Christmas v. Russell*, 14 Wall. (U. S.) 84: "An agreement to pay out of a particular fund, however clear in its terms, is not an equitable assignment. A covenant in the most solemn form has no greater effect. The phraseology employed is not material provided the intent to transfer is manifested. Such an intent and its execution are indispensable. The assignor must not retain any control over the fund, any authority to collect, or any power of revocation. If he do, it is fatal to the claim of the assignee. The transfer must be of such a character that the fund holder can safely pay, and is compellable to do so, though forbidden by the assignor. When the transfer is of the character described, the fund holder is bound from the time of notice."

Compare, *Trust v. Child*, 21 Wall. 441 (U. S.): "It is well settled that an order to pay a debt out of a particular fund belonging to the debtor gives to the creditor a specific equitable lien upon the fund, and binds it in the hands of the drawee. * * * But a mere agreement to pay out of such fund is not sufficient. Something more is necessary. There must be an appropriation of the fund pro tanto, either by giving an order or by transferring it otherwise in such a manner that the holder is authorized to pay the amount directly to the creditor without the further intervention of the debtor."

Compare, *Speckman v. Smedley Bros.*, 18 A. B. R. 717, 153 Fed. 771 (D. C. Pa.): "There was some loose testimony about an 'arrangement' by which the defendants were to be paid their full claim of \$5,400 when the United States paid the final balance due to the bankrupt, but it is clear that no definite amount was agreed upon that the 'arrangement' was not recognized by the United States; and that the bankrupt never lost his control over the fund. Evidently, the bankrupt merely promised to pay the defendants when he received this balance, and the disbursing officer of the government merely promised to notify the defendants when the settlement was to be made, so that they might be present at that time. A check for \$5,000 was made payable to the bankrupt, who refused to pay more, and it is, I think, quite clear that the 'arrangement' was nothing more than the usual promise of a debtor to pay when he shall be in funds, followed by the creditor's effort to hold him up to his promise, and by the debtor's effort to get off with as small a payment as possible. Such an 'arrangement' falls short of being an enforceable equitable assignment. When the defendants really set out to obtain a valid assignment, the testimony in reference to another claim against the bankrupt shows that they knew what they needed."

fund within four months of proceedings in bankruptcy, such payment shall be deemed to be preferential, and voidable at the suit of a trustee."

[1867] In re Connor, 1 Low 532, 6 Fed. Cases 315: "By our law, it is not sufficient answer that an oral agreement to give security at some indefinite future period, if demanded, was made at the time the debt was contracted. Such an agreement, resting only in oral contract, without possession of the property, or any such circumstances as would create a legal or equitable lien, cannot be enforced against the assignees after bankruptcy, nor make a conveyance, before bankruptcy but after insolvency, legal, which would otherwise be a preference."

Thus, a depositor's agreement for a lien is thus voidable, if it takes effect within the four months.⁴⁷

But an agreement at the time of delivery to execute a lease or written conditional sales contract, which is not acted upon until within the four months' period, does not come within this rule, since it is not a "transfer" out of the insolvent fund at all, but a "reservation" of title, all the while.⁴⁸ Even though recording be required and such recording be not made until within the four months the transaction will be unimpeachable, unless the property come into the custody of the bankruptcy court before the recording of the instrument, when another principle will come into play, namely, that such custody will operate as a levy of process.⁴⁹

Thus, also, as to the identification and separation of chattels within the four months to bring them under a chattel mortgage executed before the four months.^{49a}

First Nat'l Bk. of Holdredge v. Johnson, 10 A. B. R. 208, 68 Neb. 641: "If the cattle seized and sold were—as there is much in the evidence to suggest—merely part of a larger number of cattle in the feed lots of the mortgagor at the time the instrument was executed, and were not at that time in any way separated or identified, but afterwards and within four months of bankruptcy, and while the mortgagor was insolvent, they were separated or identified through the seizure made by the bank, and the mortgagor acquiesced in such separation and identification, and expressly or by acquiescence agreed that the mortgage should apply to them, it is obvious that the lien was created then for the first time, and that there was a preference within the meaning of § 60 of the Bankruptcy Act."

47. In re Mandel, 10 A. B. R. 774 (D. C. N. Y.): A depositor in a bank, on opening his deposit agreed that all deposits should be subject to a lien in favor of the bank for any money that might be loaned to him. The date of the bank's taking possession under the agreement not the date of the agreement itself controls on the question of preferences. This case is distinguished in In re Hunt, 14 A. B. R. 425 (D. C. N. Y.). Contra, obiter, Tomlinson v. Bk. of Lexington, 16 A. B. R. 632 (C. C. A. N. Car.).

48. Compare, apparently and only impliedly, In re Hutchins Co., 24 A. B. R. 647, 179 Fed. 864 (D. C. N. Y.).

49. Bankr. Act, § 47 (a) (2).

49a. But see First Nat'l Bk. v. Penna. Bk., 10 A. B. R. 782, 124 Fed. 968 (C. C. A. Pa.): "The effect of a remarking of the billets was not to create a new lien, nor to acquire a preference for an antecedent debt between the parties. The lien acquired August 30, 1901, had not been lost, because no rights of third parties had intervened. The bank, under its contract, had a right of possession to the billets as security for the payment of debt, and could not be held guilty of securing a preference by exercising that right within four months preceding bankruptcy."

Agreements for liens for future advances to help keep the business afloat, the same to become operative on failure to repay, becoming operative within the four months, give rise to voidable preferences.⁵⁰ A chattel mortgage executed in blank before the four months period, but not filled in with the amount of the debt until within the four months period, does not take effect until the filling in and is voidable as a preference.⁵¹

Thus, as to agreements for pledge.⁵²

In *re Sheridan*, 3 A. B. R. 554, 98 Fed. 406 (D. C. Pa.), distinguished in *In re Hunt*, 14 A. B. R. 424 (D. C. N. Y.): "The goods here were never actually pledged until the exceptant, for the first time, took them into his possession a few days before the petition was filed. Before that time there was a mere agreement to pledge. The goods were never delivered to the exceptant, nor (assuming, for present purposes, that this would have been good against the other creditors) were they even set apart and continuously treated as his property. Under the facts proved, the pledge was not completed until the date of removal. *Lucketts v. Townsend*, 49 Am. Dec. 730, note. This being so, the exceptant's title attached upon that date, and the transfer created a preference in violation of the act."

Iron & Supply Co. v. Rolling Mill Co., 11 A. B. R. 200, 125 Fed. 974 (D. C. Ala.), distinguishing in *Wilder v. Watts*, 15 A. B. R. 60, 138 Fed. 426 (D. C. S. C.): "They were never actually pledged to the bank until the transfer on the 28th day of February, 1903. Before that time there was a mere agreement to pledge. The accounts were never delivered to the bank, or set apart and treated as its property, until that day. The pledge was not completed until the date of the transfer."

Thus, also, as to agreements to insure, or to assign insurance policies, or insurance money.⁵³

Long v. Farmers' Bk., 17 A. B. R. 103 (C. C. A. Iowa): "It does not purport to assign the policies of insurance, but agrees to assign an amount as collateral security sufficient to liquidate the indebtedness to the bank, 'to be applied for this purpose in case of loss by fire.' By the last paragraph it was clearly contemplated by the parties that Wells should retain possession of the policy, and in case of loss he should make the proofs, settle with and collect from the insurance company, and pay over so much of the amount collected as would be sufficient to liquidate the debt to the bank, with authority to compromise with the insurance company, but at a sum not less than the amount of the bank's claim against him. Clearly this did not constitute an assignment of the policies in presenti. This contract was no more than the personal agreement

50. *Matthews v. Hardt*, 9 A. B. R. 373, 76 N. Y. Sup. 134, distinguished in *In re Hunt*, 14 A. B. R. 424, 137 Fed. 694 (D. C. N. Y.).

51. In *re Barrett*, 6 A. B. R. 48 (D. C. N. Y.). To same effect, *Forbes v. Howe*, 3 A. B. R. 475, 102 Mass. 427.

52. *Matthews v. Hardt*, 9 A. B. R. 373, 76 N. Y. Sup. 134, distinguished in *In re Hunt*, 14 A. B. R. 416, 137 Fed. 694 (D. C. N. Y.). Contra, *In re Automobile Livery Service Co.*, 23 A. B.

R. 799, 176 Fed. 792 (D. C. Ala.), quoted at § 1372.

53. In *re Klingman*, 4 A. B. R. 254, 101 Fed. 691 (D. C. Iowa); apparently contra, *In re Veneer & Panel Co.*, 6 A. B. R. 271, 108 Fed. 593 (D. C. Wis.), affirmed sub. nom. *McDonad v. Daskam*, 8 A. B. R. 543, 116 Fed. 276; apparently contra, *In re Grandy & Son*, 17 A. B. R. 206 (D. C. S. C.). See ante, §§ 1150, 1253.

or undertaking of Wells that he would keep the property insured, and in case of loss he would collect and pay over to the bank sufficient to liquidate the debt. The contract conveyed nothing. At most it was but an executory agreement to create a lien upon a fund to arise in case of loss and collection made from the insurance company, when for the first time an equitable lien on the fund would attach. In other words, its effect was a direction to pay in case of loss. Such an agreement, while enforceable inter partes, was not binding upon either the insurer or those claiming an interest under the insured without notice of such lien. *Ellis et al. v. Kreutzinger et al.*, 27 Mo. 311, loc. cit. 314, 72 Am. Dec. 270."

Thus, also, an order by a contractor on the owner to pay a materialman, which was not presented until within the four months of the contractor's bankruptcy, being withheld by agreement not to be presented unless the contractor failed to keep up payments, is a preference as of the date of the presentation.⁵⁴ And, on the same principle, levies under irrevocable powers of attorney to confess judgment, where the power was made more than four months before bankruptcy but not acted upon until within the four months, are void, if otherwise preferential.⁵⁵

Likewise, an agreement entered into before the four months to give a lien or make any other transfer, not acted upon until later, may constitute a transfer as of the date of the actual fulfillment of the agreement and be a preference within four months.⁵⁶

Vitzthum v. Large, 20 A. B. R. 666, 162 Fed. 685 (D. C. Iowa): " * * * if it was transferred to the bank within the four months immediately preceding the bankruptcy, to apply upon a prior debt of the bankrupt, though in pursuance of an agreement made with him prior to said four months that he would do so, it would seem to fall within the rule held by the Court of Appeals, in *Long v. Farmers Bank* (supra) and *In re Great Western Mfg. Co.* (supra)."

But the possessing one's self of material, within the four months, and the selling of the same under a subsisting contract made before the four months, has been held not to be a preference:

Savin v. Camp, 3 A. B. R. 579, 98 Fed. 974 (D. C. Ore.), rejected in *Torrance v. Winfield Bk.*, 11 A. B. R. 185 (Sup. Ct. Kas.): "The transfer by the Colby Company to Camp was not a preference under the Bankruptcy Act. It is true, the transaction was consummated within the four months, but it originated in October, 1897. What was done was in pursuance of the pre-existing contract, to which no objection is made. Camp furnished the money out of which the property which is the subject of the sale to him was created. He had good right, in equity and in law, to make provisions for the security of the money so advanced, and the property purchased by his money is a legitimate security and one frequently employed. There is always a strong equity in favor of a lien by one who advances money upon the property which is the product of the money so ad-

⁵⁴. *Johnston v. Huff*, 13 A. B. R. 287, 133 Fed. 704 (C. C. A. Va.), discussed and distinguished in *Wilder v. Watts*, 14 A. B. R. 60 (D. C. S. C.).

⁵⁵. *Wilson v. Nelson*, 7 A. B. R. 142, 183 U. S. 198.

⁵⁶. See ante, § 1326½.

vanced. This was what the parties intended at the time, and to this, as already stated, there is, and can be, no objection in law or in morals. And so when, at a later date, but still prior to the filing of the petition in bankruptcy, Camp exercised his rights under this valid and equitable arrangement to possess himself of the property and make sale of it in pursuance of his contract, he was not guilty of securing a preference under the Bankruptcy Law."

And where there exists a bona fide contract of purchase of the entire output of the bankrupt's lumber mill, the delivery of lumber thereunder, within the four months and when the seller was known to be insolvent, is not a preference, even though part of the purchase price already had been advanced.⁵⁷

Again, the mere transmitting of actual possession within the four months where there has been a previous sufficient setting apart (though on the debtor's own premises), to constitute a pledge or mortgage or declaration of trust before the four months, will not bring the "transfer" within the four months period.⁵⁸

Sexton v. Kessler & Co., 21 A. B. R. 807, 172 Fed. 535 (C. C. A. N. Y.): " * * * it [the Supreme Court] also states this underlying and controlling distinction: The exercise of a pre-existing right well founded in equity is not a preference, although occurring within the prescribed period; 'the bald creation of a lien within four months' is a preference. The application of the principle involved in this distinction is decisive here in favor of the Manchester house. It had an equitable right to the securities which were held 'in escrow' for its benefit, its rights and equities were created years before the bankruptcy; it could at any time have enforced its right to the possession of the securities; no element of fraud and no intervening rights of purchasers or attaching creditors appear; the securities were not property, the possession of which would be visible to third persons and afford a basis of credit. It is my opinion that possession was taken pursuant to a pre-existing right, and that equitable principles support such right. I think that this is in no aspect a case of the bald creation of a lien within four months of bankruptcy. The case of *Zartman v. First National Bank*, 189 N. Y. 273, 19 Am. B. R. 27, * * * is not in conflict with these views. In that case there was merely a contract to give a mortgage upon after-acquired property. There was no lien which could have been enlarged or perfected by taking possession."

Also, a bankrupt contractor's unrecorded indemnity agreement to the surety on his bond, whereby he agrees, in the event of inability to complete the contract, to assign "and does hereby assign" to the surety the plant dedicated to the job, has been held valid, although the material, etc., included in the "plant," was not acquired by the contractor until afterwards, the court placing the decision on the doctrine of *Thompson v. Fairbanks*, 196 U. S. 517, that the lien being good between the parties, was good against the trustee.

⁵⁷. *Mills v. Virginia-Carolina Lumber Co.*, 20 A. B. R. 750, 164 Fed. 168 (C. C. A. N. Car.).

⁵⁸. *Sexton v. Kessler*, 225 U. S. 90,

28 A. B. R. 85 (quoted at length at § 1146, affirming *Sexton v. Kessler*, 21 A. B. R. 807, 172 Fed. 535). Also, compare ante, § 1146, and post, § 1372.

Wood v. U. S. Fidelity & Guaranty Co., 16 A. B. R. 25, 143 Fed. 424 (D. C. Mass.): "The auditor finds that at the time the indemnity agreement was executed, King had not begun the contract work and that no part of the plant or material taken was then at Ft. McKinley. It does not appear when the plant or material taken was acquired by King nor when it was taken to Ft. McKinley. Assuming that it was all acquired by King after the execution of the indemnity agreement, the defendant's claim to it when it was taken was, in my opinion, none the less valid. The defendant's right to the property is still, as in *Thompson v. Fairbanks*, 196 U. S. 517, 13 Am. B. R. 437, and *Humphrey v. Tatman*, 198 U. S. 91, 14 Am. B. R. 74, to be judged not by the state of facts existing when possession was taken, but by the state of facts existing when the right was given. Since possession was taken before the bankruptcy, the defendant, upon taking possession, held the property by a title relating back to the time when its right was acquired, at which time, so far as appears, there was nothing to prevent King from giving it such a right, and by a title which is good against the trustee in bankruptcy." This decision might equally as well have been based on the doctrine that the lien given was a present transfer ["does hereby assign"] operative immediately on acquisition of the after-acquired material, etc.

And where the transaction is a present lien and not an agreement to give a lien it will be supported, so far as this element of a preference is concerned.⁵⁹

§ 1370 $\frac{1}{4}$. Ratification within Four Months of Prior Ineffectual Transfer.—Perhaps the ratification, within the four months, of a prior ineffectual transfer would follow the same principle, for the title is not actually parted with until within that period, and the doctrine of reverter to the original date is no stronger, as against creditors, than in the case of agreements for liens. However, this point has not been decided clearly as yet.⁶⁰

§ 1370 $\frac{1}{2}$. Assignment of Accounts before but Collections within Four Months.—Where an assignment of accounts was made by an insolvent debtor to a creditor before the four months period the transaction will not be a preference because of the fact that the accounts are collected within the four months period.⁶¹

Lowell v. International Trust Co., 19 A. B. R. 853, 158 Fed. 781 (C. C. A. Mass.): "One of the counts of the declaration is based on the receipt by the International Trust Company within four months of the filing of the petition in bankruptcy, of funds coming from certain accounts which had been assigned to it before that period commenced. It is difficult to perceive on what ground this claim rests, because the substantial rights of the parties were fixed at the time the assignment was made, and the collections were only incidents thereof."

§ 1370 $\frac{3}{4}$. Pledge, etc., before, but Sale within Four Months.—If a transfer by way of pledge is not preferential, because of being made

⁵⁹. Compare, *In re First Nat'l Bk. of Louisville*, 18 A. B. R. 766, 155 Fed. 100 (C. C. A. Ky.).

⁶⁰. See ante, § 1326 $\frac{3}{4}$.

⁶¹. *In re Francis J. Bird*, 25 A. B. R. 24, 180 Fed. 229 (D. C. Minn.).

outside of the four months period, the subsequent sale of the subject matter of such pledge does not create a preference.

First Nat. Bank v. Lanz, 29 A. B. R. 247, 202 Fed. 117 (C. C. A. La.): "The pledge of bank stock having been given to and received by the bank more than four months before bankruptcy, it cannot be held to be a preference, though given to secure a pre-existing, unsecured, debt. The sale within four months, pursuant to the pledge, would not affect the result. *Jerome v. McCarter*, 94 U. S. 734."

§ 1371. "After-Acquired Property" Taken Possession of by Mortgagee within Four Months.—And it would seem on principle that where "after-acquired property" is acquired within the four months period and possession is thereafter taken under a chattel mortgage attempting in terms to cover after-acquired property, such taking of possession would operate to fix the lien as of the date of the taking of possession, at least of the after-acquired property, and would amount to a preference as of such date; but such is not the holding where the State law declares that the lien under such circumstances reverts to the date of the original mortgage.⁶²

§ 1372. Equitable Liens Not Requiring to Be Recorded, Good.—On the other hand, equitable liens not required to be recorded, made by oral or written contract on present consideration, or before the four months period, upon choses in action or other property, may be good although actual delivery to the creditor be not made until within the four months period, if there be the equivalent of a delivery;⁶³ or if there be not the

62. *Thompson v. Fairbanks*, 13 A. B. R. 437, 196 U. S. 516, rejecting, *In re Ball*, 10 A. B. R. 564, 123 Fed. 164 (D. C. Vt.); *In re Rogers & Woodward*, 13 A. B. R. 82, 132 Fed. 560 (D. C. Vt.); *In re Nat'l Valve Co.*, 15 A. B. R. 524 (D. C. Ohio); *Wood v. U. S. Fidelity & Guaranty Co.*, 16 A. B. R. 25, 143 Fed. 424 (D. C. Mass.); *Fisher v. Zollinger*, 17 A. B. R. 618, 149 Fed. 54 (C. C. A. Ohio). See also, subdiv. "C" of the preceding division of this chapter, § 1236.

In Rhode Island an equitable lien or charge upon after-acquired property arises as soon as the property is acquired, *In re Chantler Cloak & Suit Co.*, 18 A. B. R. 498, 151 Fed. 952 (D. C. R. I.). But compare, *In re White*, 22 A. B. R. 200 (Ref. R. I.).

63. See ante, §§ 1150, 1253, 1253½, 1298, 1370; compare, § 1146. *In re Francis J. Bird*, 25 A. B. R. 24, 180 Fed. 229 (D. C. Minn.). Compare, though more than equitable lien, *Sexton v. Kessler & Co.*, 28 A. B. R. 85, 225 U. S. 90, quoted at § 1146.

McDonald v. Daskam, 8 A. B. R. 543, 116 Fed. 276 (C. C. A. Wis., affirming *In re Veneer & Panel Co.*, 6

A. B. R. 271, 108 Fed. 593, D. C. Wis.), where a parol agreement made before the four months period that certain fire insurance policies should stand as collateral for an antecedent debt, was held to create an equitable lien upon the proceeds of the policies, although actual delivery of the policies to the creditor was not made until within the four months period, the custody of the insurance agent being evidently considered by the parties as a sufficient delivery.

But compare *Long v. Farmers' Bk.*, 17 A. B. R. 103 (C. C. A. Ia.). And compare *In re Klingman*, 4 A. B. R. 254, 101 Fed. 691 (D. C. Ia.). Perhaps *Wood v. U. S. Fidelity & Guaranty Co.*, 16 A. B. R. 25, 143 Fed. 424 (D. C. Mass.), quoted in preceding section. Compare, *In re Duncan*, 17 A. B. R. 289 (D. C. S. Car.), where the court proceeds upon the erroneous theory that the property was in custodia legis by the filing of the bankruptcy petition, although before adjudication and when no receiver had been appointed. See post, "What Constitutes Custodia Legis," § 1524.

Compare, as to "equitable assign-

equivalent of a delivery.⁶⁴

Wilder v. Watts, 15 A. B. R. 57, 138 Fed. 426 (D. C. S. C.): "The testimony supports the answer of the defendant Watts that the money was advanced to him in good faith at a time when he was solvent, to be used in his business; that there was an agreement at that time that his stock of goods was to be insured, and that the policies were to be assigned as security for the loan. There was a present consideration, and an agreement to assign the policies, which, on principle and on authority, created an equitable lien upon the money due on the policies of insurance. * * * The general doctrine is that where a party by express agreement sufficiently indicates an intention to make some particular property, real or personal, or fund, a security for a debt or other obligation, and promises to assign or transfer the property as security, equity, regarding that as done which ought to be done, creates an equitable lien upon the property indicated. * * * The fact that the policies of insurance were not actually delivered to the creditors is of no consequence here. A case might arise in which delay or nondelivery might be important as evidence upon the question of a complete execution of the agreement for a lien, but the testimony shows beyond dispute the agreement for a lien; and equity, which regards the true intention of the transaction, will consider what was actually done as sufficient if the parties themselves treated it as a sufficient performance of that part of the agreement. 'Actual delivery of the policies and continuous possession by the transferee are not indispensable to create and preserve such lien as is now being considered.' *Spring v. Ins. Co.*, 8 Wheat. 268, 5 L. Ed. 614. As most of the standard forms of policies inhibit their assignment before a loss, the actual manual delivery of the policy after the loss suffices."

In *re Grandy & Son*, 17 A. B. R. 206, 146 Fed. 318 (D. C. S. C.): "Mrs. Grandy's right and title to these policies accrued at the moment when she as-

signed them." In *re Faulhaber Stable Co.*, 22 A. B. R. 381, 170 Fed. 68 (C. C. A. N. Y.), wherein it was held that a receipt given to an auctioneer for moneys advanced to the owner and for expenses incurred and authorizing the auctioneer to deduct the same from the proceeds of sale did not constitute an equitable assignment, where the auction sale never took place and the actual sale was made several months afterwards by the trustee in bankruptcy, the court saying: "It is quite plain that the petitioner had no right in the chattels as pledgee, because there was no change of possession, nor as mortgagee, because no mortgage was filed, as is required by § 90 of the Lien Law (chapter 418, p. 536, Laws N. Y. 1897), regulating chattel mortgages. Nor had it any equitable lien on the actual proceeds of sale. If the authority given in the receipt to the petitioner to deduct the advances from the proceeds of sale could be construed as assignment cognizable in equity, rather than as a promise to pay to be enforced at law, still no such fund ever came into existence. The actual sale was made six months

later by order of a different person, viz., the trustee, through another auctioneer. If it were within the power of a court of equity to impress the proceeds of sale inter partes with an equitable lien, such a power would not be exercised to the prejudice of creditors. In bankruptcy, equality is equity."

Also compare, *In re Farmers Supply Co.*, 22 A. B. R. 460, 170 Fed. 502 (D. C. Ohio). Also compare, where an equitable assignment was upheld, *Godwin v. Murchison Nat'l Bk.*, 22 A. B. R. 703, 145 N. Car. 320.

Compare, as to "equitable" liens, *Warehousing Co. v. Hand*, 16 A. B. R. 63, 143 Fed. 32 (C. C. A. Wis., affirmed sub nom. *Security Warehousing Co. v. Hand*, 19 A. B. R. 291, 206 U. S. 415); also, *Fourth St. Nat'l Bk. v. Millbourne Mills Co.*, 22 A. B. R. 442, 172 Fed. 177 (C. C. A. Pa.), quoted at § 1146.

Equitable Lien Defined.—In *re Max Goldman*, 23 A. B. R. 497, 174 Fed. 579 (C. C. A. Ohio), quoted at § 1878.

64. Compare, to same effect, *Hanson v. Blake*, 19 A. B. R. 325, 150 Fed. 342 (D. C. Me.).

signed her renunciation of dower, which was the consideration paid. Equity from that date would have compelled the execution of such formal papers as were necessary to enable her to obtain her own, and in such circumstances the date of the formal assignment does not seem to me material. All transactions between a wife and a husband, who afterwards proves to be in failing circumstances ought to be subject to the closest scrutiny by the courts, and no claim by her upon his estate, unless sustained by abundant testimony, ought to be allowed; but in this case there is no question of the absolute good faith of this transaction. That she has parted with a valuable property right upon an express agreement that a specific security should be assigned to her, and the neglect of the husband to make the formal assignment—a neglect for which she is not to be blamed, and which did not work to the prejudice of the creditors—ought not to operate to defeat her title.”

Such was the holding where a New York house had set apart in its own vaults securities in favor of a foreign concern as a basis for drafts, with the stipulation to keep the amount of them continually good, by substitution, and then, within the four months before its bankruptcy and under circumstances indicating plainly to the foreign concern that disaster was impending, had delivered the securities to the foreign concern, part of the court so holding on the theory that a declaration of trust had been made by the New York house, the remainder of the court on the theory that the securities had been both pledged and mortgaged and that the sending of the securities to the foreign house within the four months period did not create a lien but merely enlarged or perfected one already pre-existent.⁶⁵

Such also was the holding as to an oral agreement made before the four months period that the bankrupt's timber and timber contracts should stand as security for advances and supplies, and the equitable lien so created was held to attach also to the proceeds of sale.⁶⁶

Thus an equitable lien for advances made on lumber to be manufactured has been upheld.

Gage Lumber Co. v. McEldowney, 30 A. B. R. 251, 207 Fed. 255 (C. C. A. Ky.): “At the date of the contract the lumber had not been manufactured; but the contract required its manufacture and its distinctive character identified it with its purchasers. * * * Upon the theory that title to the lumber passed to the Gage Company—that is, on the current deliveries it was simply receiving its own property—there was no occasion to pay anything, and each of these 50 per cent payments was a new advance; but, treating the contract as one of equitable lien, this complication disappears and the original advances, so far as unpaid, always remained a lien on all the undelivered lumber manufactured thereunder.

“A court of bankruptcy views transactions of this kind upon the broadest equitable principles; and does not hesitate to effectuate the actual intent of transactions honestly had with a bankrupt, without much restraint as to formality or procedure (*Hurley v. Atchison, Topeka & Santa Fe Ry.*, supra, at p. 132, approving language of Circuit Judge Putnam). When we regard the substance

⁶⁵ *Sexton v. Kessler & Co.*, 21 A. B. R. 807, 172 Fed. 535 (C. C. A. N. Y.), quoted at § 1372.

⁶⁶ *Goodnough Stock Co. v. Gallo-way*, 22 A. B. R. 803, 171 Fed. 940 (D. C. Ga.).

and effect of the present transactions, apart from their form, it is reasonably plain that the Clairfield Company would not be heard to say that the Gage Company did not, through its advances and the other company's actual production and stacking of the lumber, acquire an interest, certainly an equitable interest, in this lumber. The essence of the purchaser's right was the fact, constantly to be remembered, that each advance was made for the very purpose of having a particular thing produced. The last analysis of such a transaction is that when the lumber was produced and placed on sticks it was in effect appropriated toward the payment of the loan as required and promised under the contract.

"It is true that in the negotiations leading up to the contract, efforts were made, which failed, to have the lumber as it was piled marked with the name of the Gage Company, also to have a lease made to that company of part of the yard upon which to set aside the lumber as it was manufactured; the representatives of the Clairfield Company expressing as to the one plan, fears that it would injure the credit of the company, and, further, that they did not wish Mrs. Anderson, the president of the company, to know of the advances; * * * but (aside from any question of admissibility of such statements) these features of the negotiations concerned an endeavor of the Gage Company to secure a transfer to it of the title to the lumber as fast as it was produced * * * and while it must be conceded that in one sense such statements would seem to be opposed to a purpose to create an equitable lien, yet no charges of fraud or bad faith are made respecting either the negotiations or the contract; * * * To say, then, that such antecedent negotiations are inconsistent with the idea of an equitable interest in the lumber, is to urge that the repeated use of the words "to put on sticks to apply on our contract" is meaningless; in a word, it is to destroy the most significant portions of the contract."

The giving of a mortgage within the four months period for a pre-existing debt, in pursuance of an agreement to give it made anterior to the four months period and at the time the debt was created, cannot be sustained on the doctrine of an "equitable lien" succeeded by a mortgage, where the other elements of a preference exist.⁶⁷

It has been sought to express the doctrine of the consummating of equitable liens within the four months period as follows: The exercise of a pre-existing right, well founded in equity, is not a preference, although occurring within the prescribed period, it being the "bald assertion" of a lien within the four months that is a preference.

Sexton v. Kessler & Co., 21 A. B. R. 807, 172 Fed. 535 (D. C., affirmed by C. C. A. in 21 A. B. R. 807, 172 Fed. 535, quoted at § 1370; also affirmed by Supreme Court, 225 U. S. 90, 28 A. B. R. 85, quoted at § 1146): "While the Supreme Court in the cases referred to treats the validity of the mortgages and the rights of the mortgagees thereunder to be matters of local law, in my opinion it also states this underlying and controlling distinction. The exercise of a pre-existing right well founded in equity is not a preference, although occurring within the prescribed period; 'the bald creation of a lien within four months is a preference.'"

In *re Automobile Livery Service Co.*, 23 A. B. R. 799, 176 Fed. 792 (D. C. Ala.): "If the decisions of the State court hold transactions to create valid liens in cases in which delivery is made subsequent to the agreement to give

⁶⁷. In *re White*, 22 A. B. R. 200 (Ref. R. I.). Also, see ante, § 1370.

the lien but before the right of intervening creditors has been fastened upon the property, the delivery of the property, under such circumstances, will not constitute an illegal and voidable preference under the bankruptcy law. * * * In view of the principle asserted by these cases, it seems to me that the exercise of the right to take possession of the pledged property, within the four months, did not constitute an illegal preference, because it was done pursuant to a valid agreement to pledge for which a present consideration moved to the bankrupt, and therefore related back to such agreement, except as against intervening claimants who had perfected liens on the pledged property in the interim, of whom there were none."

§ 1372½. **Conditional Sales Contracts.**—A conditional sale, unless a mere disguise, is not a "transfer" out of the insolvent fund at all, but is a mere reservation of title to property not yet become part of such fund; therefore, it cannot be a preference, and, a fortiori, the recording of it could not operate as a transfer nor could the failure to record it effect a transfer of the title to the conditional vendee.⁶⁸

§ 1373. **State Law Governs as to Time Agreements for Liens, and Taking of Possession or Recording or Acquisition of Property Take Effect as Liens or Other Transfers.**—But the state law will govern as to the time that agreements for liens take effect as liens, also, as to whether the taking of possession under an unrecorded instrument, or the recording of such instrument, reverts to the date of the original transaction, or effects a transfer as of the date of the taking of possession or recording.⁶⁹

Thompson v. Fairbanks, 13 A. B. R. 437, 196 U. S. 516: "Whether, and to what extent a mortgage of this kind is valid is a local question, and the decisions of the State Courts will be followed by this court in such case."

In *re Hunt*, 14 A. B. R. 427, 139 Fed. 283 (D. C. N. Y.): "It must be borne in mind in considering these questions that the effect of mortgages and acts

⁶⁸. Compare ante, §§ 1244 and 1334¾.

⁶⁹. See discussions in the following paragraphs, ante, § 1139, et seq., and § 1237. *Fisher v. Zollinger*, 17 A. B. R. 625, 149 Fed. 54 (C. C. A. Ohio); In *re Newton*, 18 A. B. R. 567, 153 Fed. 841 (C. C. A. Ark.), quoted at §§ 1263, 1381; In *re Reynolds*, 18 A. B. R. 666, 153 Fed. 295 (D. C. Ark.), quoted on other points at §§ 1246½, 1381; *Jones v. Coates*, 28 A. B. R. 249, 196 Fed. 860 (C. C. A. Mo.), decided under the law of Kansas. Compare discussion in *Hanson v. Blake*, 19 A. B. R. 325, 150 Fed. 342 (D. C. Me.). Instance, In *re Dundore*, 26 A. B. R. 100 (D. C. Pa.).

Compare, In *re Automobile Livery Service Co.*, 23 A. B. R. 799, 176 Fed. 792 (D. C. Ala.), quoted at § 1372, wherein the court applies the doctrine of §

1373 in such a way as to make a mere agreement to give a pledge, not consummated by delivery until within the four months, "revert" to the date of the agreement, which, it is considered by the author, is a misapplication of the principle.

Instance, **after-acquired property coming under chattel mortgage.** In Vermont possession taken within the four months period reverts to original date of mortgage. *Thompson v. Fairbanks*, 13 A. B. R. 437, 196 U. S. 516. Compare, In *re Ball*, 10 A. B. R. 564, 123 Fed. 164 (D. C. Vt.), rejected by *Thompson v. Fairbanks*, 13 A. B. R. 437, 196 U. S. 516.

Instance, **after-acquired property coming under agreement for indemnity lien**, *Wood v. U. S. Fidelity & Guaranty Co.*, 16 A. B. R. 25, 143 Fed. 424 (D. C. Mass.).

under them in transferring title, etc., is a local question, and the courts of the United States must follow the decisions of the highest court of the State."

Compare, analogously, *In re Engle*, 5 A. B. R. 373, 105 Fed. 893 (D. C. Pa.): "The bonds accompany and are secured by a mortgage, and it is argued in support of the validity of the executions that the lien of the judgments is carried back by the law of Pennsylvania to the date when the mortgage was recorded, and should, therefore, be considered as if the lien had originated at that time. This may be true for certain purposes, but, under the present circumstances, I must decline to assign a fictitious date to the existence of the lien."

Likewise, it governs as to the time the lien attaches to after-acquired property.⁷⁰

In re Chantler Cloak & Suit Co., 18 A. B. R. 498, 151 Fed. 952 (D. C. R. I.): "The latter case [*Thompson v. Fairbanks*, *supra*] also decides that, on the question of the validity of a mortgage upon after-acquired property, the federal court will follow the decisions of the State court. Under Rhode Island decisions, an equitable lien or charge upon the after-acquired property arose as soon as the property was acquired."

§ 1374. Mere Exchanges of Property of Equal Value within Four Months, Not Preferences.—The mere exchange of property of equal value within the four months will not constitute a preference; nor will the renewal of securities of equal value; but if the property last given exceeds the value of the property for which it is exchanged, a preference will exist as to the excess; but the exchange will only be voidable as a preference to the extent of such excess.⁷¹

§ 1375. Four Months—How Computed.—The four months are to be computed by excluding the day the preference was given or recorded, and including the day the petition is filed; but the reverse method is harmless error.⁷²

Fractions of a day are to be considered;⁷³ and it is the time of the filing of the petition, not of the issuance nor service of the subpoena that controls.⁷⁴

§ 1376. Preferences Made before Bankruptcy Act Passed, Voidable.—Preferences made before the passage of the Bankruptcy Act are voidable, if made within four months of the filing of the petition. Of course this situation under the present act could only arise in the case of

⁷⁰. Compare, *Hanson v. Blake*, 19 A. B. R. 325, 150 Fed. 342 (D. C. Me.).

⁷¹. *In re Cutting*, 16 A. B. R. 753, 145 Fed. 388 (D. C. N. Y.). As to all these several propositions, see ante, "First and Third Elements of a Preference," §§ 1295, 1320, et seq.

⁷². Bankr. Act, § 31 (a); *Whitley Grocery Co. v. Roach*, 8 A. B. R. 505, 115 Ga. 918; *Dutcher v. Wright*, 94 U.

S. 553; *In re Dupree*, 97 Fed. 28; *In re Stevenson*, 2 A. B. R. 66, 94 Fed. 110 (D. C. Del.); *In re Planing Mill Co.*, 6 A. B. R. 38 (Ref. N. Y.).

⁷³. *In re Planing Mill Co.*, 6 A. B. R. 38 (Ref. N. Y.); apparently contra (analogously), *In re Hill*, 15 A. B. R. 499, 140 Fed. 984 (D. C. Calif.).

⁷⁴. *In re Lewis*, 1 A. B. R. 458 (D. C. N. Y.).

voluntary bankruptcies, since by the Act itself involuntary petitions could not be filed until four months after the Act otherwise took effect.⁷⁵

§ 1377. Preferences Made after Filing Petition if before Adjudication.—A preference may be made by the bankrupt, after the filing of the petition as well as before, if made before adjudication,⁷⁶ provided it be made with property that was transferable or leviable on at the time of the filing of the petition.

The title vests only "as of the date he was adjudged a bankrupt."⁷⁷

§ 1378. After Adjudication, No Preference.—After adjudication it is not within the power of a bankrupt to make a preference: title has passed from him.⁷⁸

§ 1379. Preferences as Affected by Recording—Amendment of 1903 and before.—Where the preference consists in a transfer, the four months period will not expire until four months after the date of the recording or registering of the transfer, if by law recording or registering is required.⁷⁹

This exception was engrafted upon the statute by the Amendment of 1903, and was engrafted in order to prevent secret preferences by way of mortgages and other liens not recorded until after the four months period had elapsed within which bankruptcy proceedings could have been brought.⁸⁰

However, it had been held, even before the law was amended in 1903, that the date of the recording or filing of a preferential chattel mortgage or other instrument would govern, notwithstanding it was executed and delivered before the four months.⁸¹ But the true rule, before the Amend-

⁷⁵. In re Brown, 1 A. B. R. 107, 91 Fed. 358 (D. C. Ore.); contra, In re Terrill, 4 A. B. R. 145 (D. C. Vt.).

⁷⁶. Bankr. Act, § 60 (a); Instance, In re Austin, 13 A. B. R. 139 (D. C. Hawaii). Compare, In re Duncan, 17 A. B. R. 289 (D. C. S. C.); In this case, however, the avoidance was placed, not upon ground of preference, but of the passing of the title by the filing of the petition.

Compare, peculiar facts in Pratt v. Columbia Bank, 18 A. B. R. 406, 157 Fed. 137 (D. C. N. Y.), wherein the transfer was made after a void petition in involuntary bankruptcy had been filed and before a supplemental valid one was filed.

⁷⁷. Obiter, In re Milk Co., 16 A. B. R. 729, 145 Fed. 1013 (D. C. Penn.).

⁷⁸. Ryttenberg v. Schefer, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.).

Instances where facts show no preference within the time limit.

1. Pratt v. Christie, 12 A. B. R. 1,

95 App. Div. 282 (N. Y. Sup. Ct. App. Div.).

² In re Folb, 1 A. B. R. 22, 91 Fed. 107 (D. C. N. Car.); Creditors receiving preferences under an assignment made more than a year before bankruptcy.

³. Batchelder & Lincoln Co. v. Whitmore, 10 A. B. R. 641 (C. C. A. Mass.); Creditor receiving secret advantage under a composition made in 1896.

⁷⁹. Bankr. Act, § 60 (a). Compare, ante, § 1334; post, § 1507.

⁸⁰. Compare, First National Bank v. Johnson, 10 A. B. R. 208, 68 Neb. 641.

⁸¹. Babbett v. Kelly, 9 A. B. R. 335, 70 S. W. 384 (St. Louis Ct. App.); In re Klingman, 4 A. B. R. 254, 101 Fed. 691 (D. C. Iowa).

Obiter, Matthews v. Hardt, 9 A. B. R. 373, 76 N. Y. Sup. 134: "The trend of the decisions in the United States Supreme Court under the recent Bankruptcy Act upon the subject of the date of the transfer, is in support of

ment of 1903, was contra, namely, that if the actual transfer took place before the four months period, it was good notwithstanding the recording or registering of the transfer occurred within the four months period.⁸² And this was the view held by the courts under the law of 1867.

Sawyer v. Turpin, 91 U. S. 118: "The conveyance was by a bill of sale absolute in its terms, having no condition or defeasance expressed, but it was understood by the parties to be a security for the debt due. It was, in substantial legal effect, though not in form, a mortgage. Having been executed more than four months before the petition in bankruptcy was filed, there is nothing in the case to show that it was invalid. True, it was not recorded, and it may be doubted whether it was admissible to record. True, no possession was taken under it by the vendee; but for neither of these reasons was it the less operative between the parties. It might not have been a protection against the attaching creditors, if there had been any; but there was none. It was in the power of Turpin to put it on record any day, if the recording acts apply to such an instrument, and equally within his power to take possession of the property at any time before other rights against it had accrued. These powers were conferred by the instrument itself, immediately on its execution."

After the Amendment of 1903 it would have seemed on principle that since the Amendment made the four months an essential element of the very definition of a preference itself, the date of the recording or filing ought to have been taken as being the date of the consummation of the transfer so far as creditors in bankruptcy were concerned, and to such effect were some of the decisions after that Amendment, even before the further Amendment of 1910.⁸³

English v. Ross, 15 A. B. R. 370, 140 Fed. 630 (D. C. Pa.): "The case turns therefore on whether the transfer of property effected by the deeds is to be judged as of the dates when they were respectively executed, or as of June 2,

the view that with respect to an instrument of transfer, it is the time when such instrument is recorded, or when possession is taken or notice is otherwise brought home to the creditors of the bankrupt that is controlling."

^{82.} In re Mersman, 7 A. B. R. 46 (Ref. N. Y.).

^{83.} See ante, "Nature of Limitation," § 1369; In re Montague, 16 A. B. R. 20, 143 Fed. 428 (D. C. Va.).

As an act of bankruptcy, however, In re Donnelly, 27 A. B. R. 504, 193 Fed. 755 (D. C. Ohio). Compare, In re Beckhaus, 24 A. B. R. 380, 177 Fed. 141 (C. C. A. Ills.), quoted at § 1383; compare, though distinguishable, In re Dundore, 26 A. B. R. 100 (D. C. Pa.); In re Beckhaus [Rasmussen v. McKay], 24 A. B. R. 389, 117 Fed. 141 (C. C. A. Ills.).

Compare, analogously, *Johnson v. Huff*, 13 A. B. R. 287, 133 Fed. 704 (C. C. A. Va.): This was a case where

an order of a contractor on funds in the owner's hands was not to be presented unless the contractor did not keep up payments; the court holding it not to be a "transfer" until presentation. Compare, In re Klingman, 4 A. B. R. 254, 101 Fed. 691 (D. C. Iowa). See note In re Wright, 2 A. B. R. 368, 96 Fed. 187 (D. C. Ga.); inferentially, contra, In re U. S. Food Co., 15 A. B. R. 329 (Ref. Mich.).

This would not be the effect of a failure to file or record a conditional sale contract, however, for such contract does not effect a transfer but simply keeps a title that never has left the original owner, preference implying transfer. *Bradley Clark & Co. v. Benson*, 13 A. B. R. 170, 100 N. W. 670 (Minn.); In re Cavagnaro, 16 A. B. R. 323, 143 Fed. 668 (D. C. N. H.). But see, In re Klingman, 4 A. B. R. 254 (D. C. Iowa). But compare, *Deland v. Miller*, 11 A. B. R. 744, 119 Iowa 368.

1903, when they were left for record; the latter only being within the four months period prior to bankruptcy, necessary to make out a preference. * * * "Having sole regard to the State law, it must be confessed that the deeds in controversy were effective to convey title, whatever their purposes, without being recorded; and, that if this is controlling, it is, to say the least, doubtful whether they can be disturbed. It is only qualifiedly, here, that recording can be said to be required. Originally under the Act of May 28, 1715, 1 Smith's Laws, 95, except as to mortgages, it was permissive merely. *Powers v. McFerreran*, 2 Serg. & Rawle, 34; *Kellar v. Nutz*, 5 Serg. & Rawle, 246. But by the Act of May 18, 1775, 1 Sm. Laws, 422, it was made compulsory, within six months, if the grantee would preserve his title as against subsequent purchasers or mortgagees, without notice, for value. * * *

"But, however, the deeds would be regarded under ordinary circumstances, and without passing upon the standing of the trustee with reference to the State law, the case turns, in my judgment, on the construction to be given to that provision of the Bankruptcy Act, and others, by which it is subtended, which, treating of voidable preferences occurring within four months of bankruptcy, prescribes (§ 60a): 'Where the preference consists in a transfer, such period of four months shall not expire until four months after the date of the recording or registering of the transfer if by law such recording or registering is required.' This was introduced by the amendatory Act of 1903, and was manifestly intended to overcome the decisions under the law as it previously stood (*In re Wright*, 2 Am. B. R. 364; *In re Mersman*, 7 Am. B. R. 46; *Dean v. Plane*, 195 Ill. 495), by which it was held the same as under the Act of 1867 (*Clark v. Iselin*, 21 Wall. 360, 375; *Sleek v. Turner*, 76 Pa. 142), that the date of the delivery of a preferential instrument, rather than the date when it was put on record, marked the beginning of the four months period, although even then, cases were not wanting which held that the date of record was to be taken. *In re Klingman*, 4 Am. B. R. 254; *Chesapeake Shoe Co. v. Seldner*, 10 Am. B. R. 466, 122 Fed. 593; *Babbitt v. Kelley*, 9 Am. B. R. 335; *Mathews v. Hardt*, 9 Am. B. R. 373; *Johnson v. Huff*, 13 Am. B. R. 287. It also must be regarded as intended to bring the section where it is found into substantial accord with § 3a, b, where, after defining what shall constitute an act of bankruptcy, and providing that proceedings must be begun within four months after the commission by the bankrupt of the act relied upon, it is declared:

"Such time shall not expire until four months after the date of the recording or registering of the transfer or assignment, where the act consists in having made a transfer of any of his property with intent to hinder, delay or defraud his creditors, or for the purpose of giving a preference as hereinbefore provided, or a general assignment for the benefit of creditors; if by law such recording or registering is required or permitted; or, if it is not, from the date when the beneficiary takes notorious, exclusive or continuous possession of the property, unless the petitioning creditors have received actual notice of such transfer or assignment."

"According to what is so provided, there would seem to be no question that, in this State, where a preferential or a fraudulent transfer, which is relied upon as an act of bankruptcy, consists in a conveyance of real estate, under which possession is not taken, and of which the petitioning creditors have no actual knowledge, it is not committed in legal intendment until the deed or other instrument by which it is accomplished is put on record. Notice is made essential, and where there is none in reality, according to the other alternative, it must be supplied constructively by recording. This is the effect of record by the State

law and is thus 'required' within the meaning of this provision. Any other view makes it insensible and useless.

"But whatever construction is thus given to the one section (§ 3a, b), is necessarily carried forward and impressed upon the other (§ 60a). The two are intimately related, the one in that particular being the basis of and dominating the other, and it is the failure to recognize this and to draw them together as they should be, that is responsible for any misapprehension. What is thus 'required' in the way of recording in the one is also 'required' as a consequence in the other, and for the same purpose. It is true that some things are omitted in the transition, but enough is retained to make this manifest. It is none other, for instance, than the preference which is made an act of bankruptcy in the earlier section that is intended to be made voidable at the instance of the trustee, in the interest of creditors, in the later, and upon substantially the same terms, the superadded condition only being present, that the person who received it had reasonable cause to believe that a preference was intended. In the present case, the petitioning creditors could unquestionably have assigned as an act of bankruptcy, the transfer of his property by the bankrupt to the defendant by the deeds in controversy, they having no knowledge of them, and the deeds having been put on record within the four months period. But if so, how can the defendant successfully deny the effect of them as a preference in his hands? The character of the transaction as a preference does not change in the shifting of the issue from the bankrupt to the preferred creditor. It may, its voidable quality dependent upon whether the creditor had reasonable cause to believe that a preference was intended. But that is another matter, and does not concern us, being unquestionably present here.

"It seems to me, therefore, clear that in any case, where the facts are the same as they are here, a deed by which a transfer of a bankrupt's property is effected, and under which no possession is taken, is to be judged, on the question of preference, by the date when it is put on record, regardless of the date of delivery; and that, tested by this, the conveyances to the defendant cannot stand. I do not lose sight of the fact that the first of these was several years prior to the passage of the Bankruptcy Act, which is not to be given a retroactive effect if it can be avoided. But the security thereby provided was a continuing one. It was not given merely for the debt then due, but also for whatever might subsequently become so; and it is safe to conclude that the original debt of \$573 is long since paid, together with whatever after that antedated the passage of the Act. Thereafter the defendant held his deeds subject to the condition there imposed, and at the risk, if not duly put on record, of having them declared void, as here upon the intervention of bankruptcy within four months after they were. If the result seems in any respect harsh, it is to be remembered that by withholding them as he did, and allowing the bankrupt to remain in full possession and enjoyment of his property, the defendant enabled him to secure a false credit, which has worked fully as much injury to others entirely innocent.

"The only doubt I have is raised by those cases which apparently hold that the right of the trustee to question such a conveyance is to be determined by the State law and what there obtains. *Thompson v. Fairbanks*, 196 U. S. 516, 13 Am. B. R. 437; *Humphrey v. Tatman*, 198 U. S. 91, 14 Am. B. R. 74, 25 Sup. Ct. Rep. 567; *In re N. Y. Economical Printing Co.*, 6 A. B. R. 615; *In re Shirley*, 7 Am. B. R. 299. But all these will be found on examination to have arisen prior to the amendments of 1903, by which the clause with regard to recording was carried forward from the third section to the sixtieth; and do not assume to pass upon the Act as it now stands. Neither do they consider the relation existing

between the two sections named. Regarding them as in these respects distinguishable, I have ventured to follow what seems to me to be the natural and necessary construction to be given to this part of the Act, upon which its efficiency in the matter of preferences, in my judgment, in large measure depends."

Compare, suggestively and obiter, *Page v. Rogers*, 21 A. B. R. 496, 211 U. S. 575 (reversing on other grounds *Rogers v. Page*): "The facts, however, do not raise the question which was argued. Upon a proper interpretation of the evidence we need not determine whether an insolvent debtor may make an agreement to convey a substantial portion of his assets to a favored creditor, keep that agreement secret for more than four months, and then execute it in fraud of the rights of his other creditors, in favor of a creditor, who then has reasonable cause to believe he is receiving a preference."

And thus a chattel mortgage, although originally given on a presently passing consideration, was, under this doctrine, held to amount to a preference, not having been filed until within the four months period, for it was not effective against creditors as a transfer until filed, and yet, at the date of filing, the consideration on which it was based was past.⁸⁴ And the rule was also held applicable to real estate transfers.⁸⁵

Indeed, the correct view of the effect of the Amendment of 1903 would seem to have been that the date of the recording or filing was thenceforth to be taken as the date of the consummation of the transfer as to creditors, since it was then and not beforehand that the creditor had effectively depleted the trust fund. In accordance with this view proof of insolvency, reasonable cause of belief and of all the other elements of a voidable preference, might properly have been made as of the date of the recording—the date of the "transfer."⁸⁶

In *re Hickerson*, 20 A. B. R. 682, 162 Fed. 345 (D. C. Idaho): "The mortgage was not recorded for nearly a year after it was executed and delivered and then just a few days before the petition in bankruptcy was filed. * * * Does the mortgage transaction, as disclosed by the record, constitute a preference under § 60a of the Bankruptcy Act? By the Amendment of 1903 * * * it is provided that, to constitute a preference, the period during which the transfer is made shall not

84. *Contra*, *Anderson v. Chenault*, 31 A. B. R. 349, 208 Fed. 400 (C. C. A. Ga.), wherein the court ignores the Amendment of 1910 to § 60b, though noting that the Amendment of 1910 to § 47a (2) would not affect the case, since the mortgage was filed before the rights of the trustee under the latter section became effective as a creditor armed with process.

85. *Ragan v. Donovan*, 26 A. B. R. 311, 189 Fed. 138 (D. C. Ohio), quoted at § 1379; also compare. *Carey v. Donohue*, 31 A. B. R. 210, 209 Fed. 328 (C. C. A. Ohio).

86. See ante, § 1334. To same effect before the Amendment of 1903, obiter, *Matthews v. Hardt*, 9 A. B. R. 373, 76 N. Y. Supp. 134, quoted at § 402, note.

[Even before Amendment of 1910 to Bankr. Act, § 60 (b).] *Mattley v. Giesler*, 26 A. B. R. 116, 187 Fed. 970 (C. C. A. Neb., reversing *Mattley v. Wolfe*, 23 A. B. R. 673, 175 Fed. 619): "Under the amended section [Amendment of 1903 to § 60 (a)] an instrument of transfer required to be recorded or registered speaks at the time the requirement is complied with and not at the time of its execution, * * *. The mortgage here, though given before, was filed within the four months preceding the commencement of the bankruptcy proceedings and the other conditions of a voidable preference being present the remaining question is whether the Nebraska statute requires such instruments to be recorded or registered."

expire until four months after the date of the recording or registering of the transfer, if by law such recording or registering is required. The mortgage 'transfer' must therefore be deemed to have been made on the 11th day of February, 1907, only five days before the filing of the petition in bankruptcy. *Humphrey v. Tatman*, 198 U. S. 91, 14 Am. B. R. 74."

[Even before Amendment of 1910 to Bank. Act, § 60 (b).] *Ragan v. Donovan*, 26 A. B. R. 311, 189 Fed. 138 (D. C. Ohio): "The court is justified, we think, in holding that the interpretation placed upon the language of Sec. 60 paragraph (a), read in connection with § 3, paragraph (b), of the Bankruptcy Act, by the cases of *English v. Ross*, *Loeser v. Bank*, and *In re Beckhaus*, should be applied to a transaction where deeds of realty are involved, as in this case, and that we should hold that the preference, manifestly attempted in behalf of the bank, should be referred for date to the time of filing the deeds."

McElvain v. Hardesty, 22 A. B. R. 320, 169 Fed. 31 (C. C. A. Mo.): "* * * the effect of the transfer to McElvain is to be judged as if made on the 7th day of July, 1905, when it was filed for record. If C. & C. were then insolvent, and if the effect of the enforcement of the transfer was to enable McElvain to obtain a greater percentage of his debt than any other of their simple contract creditors, the transfer constituted a preference within the meaning of the bankruptcy law. * * * As, for the purpose of this case the transfer is to be treated as made on the date the agreement was recorded, so the transferee's belief or cause for belief concerning it must relate to that time."

First Nat'l Bk. v. Connett, 15 A. B. R. 662, 142 Fed. 33 (C. C. A. Mo.): "The bankrupt was insolvent when he executed the mortgages and when they were recorded. The mortgages constituted a transfer of his property, and their effect was to enable the bank to obtain a greater percentage of its claims than other creditors. They were recorded within four months of the filing of the petition in bankruptcy. Therefore, assuming that a recording is required by the law of Missouri, it follows that a preference arose under § 60 (a). And, in our opinion, it also follows that the preference arose when the mortgages were recorded and not as of the date they were given. In other words, the Amendment of 1903 was intended to remedy the evil resulting from secret instruments of transfer of the bankrupt's property, the withholding of them from record until shortly before the institution of bankruptcy proceeding, and the then assertion of them as of the prior date of their execution and delivery. And this was accomplished by making the rights of a creditor thus favored determinable by the conditions existing when he caused the transfer to him to be recorded as required by the State law rather than by those existing at the time he secured it. Under the Act of 1867 not only the question of requirement to record a chattel mortgage, but also the effect of noncompliance therewith, were exclusively controlled by the law of the State. The same construction has been applied to the original act of 1898. Unless there has been some departure from this construction in its relation to voidable preferences, the Amendment of 1903 of § 60 (a), upon which subdivision 'b' thereof depends, is wholly without significance. Contrary to a presumed intent in legislative amendments it serves no purpose and performs no office whatever. Such result can be reasonably avoided by this construction of the amendment: It affects only those instruments of transfer which the State law requires to be registered or recorded; and, as to those, where there is delay, it provides that upon the question of voidable preference they shall speak as of the day of compliance with the local law and not as of the day they were given. This would preclude the application of the doctrine of relation, and it would entail a consequence upon a failure to record that

might not be imposed by the law of the State; but we deem it to be not only within the letter of the amendment, but also within the intention to correct an evil which flourished under the construction of the original act."

Nevertheless, such was not the trend of the decisions.⁸⁸ On the contrary, before the Amendment of 1910 to § 60b the weight of authority was to the effect that the Amendment of 1903 simply operated as an extension of the statute of limitations to four months after the recording, where recording was requisite, but left the proof of the different elements of a preference, insolvency, reasonable cause of belief, greater percentage, etc., to be proved as of the date of the original transfer between the parties.

Debus v. Yates, 30 A. B. R. 823, 193 Fed. 429 (D. C. Ky.): "The transfer was to be judged in determining the question of whether or not it constituted a voidable preference as of the time when it was made and not of the time of its registration and unless when it was made, the debtor was insolvent and actually intended a preference and the creditor then had reasonable cause to believe that it was so intended, it is not voidable."

Davis v. Hanover Savings Fund Soc. et al., 31 A. B. R. 368. "The reasoning and citation of authorities in *Debus v. Yates*, impresses us as they did the learned judge below. * * * Adopting this decision as the correct construction of the § 60a, as amended by the act of February 5, 1903, there is no basis for the suggestion that the mortgage was a voidable preference. The amendment of 1910 makes a radical change in the law in this respect. The mortgage in controversy here, however, was recorded in November 6th, 1909, and does not come within the provisions of that amendment. There is a saving clause in the act of 1910 preventing its application to cases pending when it went into effect, June 25th, 1910. The petition was filed here March 3d, 1910."

Rogers v. Page, 15 A. B. R. 506, 140 Fed. 596 (C. C. A. Tenn. reversed on other ground, *Page v. Rogers*, supra): "The preference in such case was given when the mortgage was executed and delivered."

In re Jackson, etc., Co., 26 A. B. R. 915, 189 Fed. 636 (D. C. Mo.), reversed on other grounds in *Sturdivant Bank v. Schade*, 27 A. B. R. 673, 190 Fed. 188 (C. C. A. Mo.): "The provision of the statute * * * was intended to postpone the time within which a transfer is open to attack as a preference * * * [it] cannot properly be so applied as to materially alter the essential character of the transaction * * * if the transfer when made was based upon a present consideration, a delay in recording the instrument does not warrant us in treating the conveyance as if it were made as security for an antecedent debt, because to do so would be to create by construction a transaction different from the actual one."

Christ v. Zehner, 16 A. B. R. 790, 212 Pa. St. 188, 61 Atl. 822: "The only question remaining, then, is as to when the title to the property of the bankrupt actually passed. Was it when the bill of sale was executed and delivered, or when possession of the goods was actually given? The authorities cited by the trial judge seem to fully sustain his conclusion that the property was transferred when the bill of sale was executed and delivered."

⁸⁸. *York Mfg. Co. v. Cassell*, 15 A. B. R. 633, 201 U. S. 342; *In re Cutting*, 16 A. B. R. 751, 145 Fed. 388 (D. C. N. Y.); *Deland v. Miller*, 11 A. B. R. 744, 119 Iowa 368. Also, see discussion, ante, § 1214.

§ 1379½. Date of Recording as Date of Preference Since Amendment of 1910.—Section 60b, relating to preferences created by instruments requiring recording, was amended in 1910, so as to make the date of the recording, wherever recording is required, to be the date at which all the various elements of the preference may be proved, at the trustee's option.

We have already seen that as the law stood, even after the Amendment of 1903, as that amendment was construed in many jurisdictions and probably according to the weight of authority, the debtor might, if solvent at the time, or if presently passing consideration had been then received, have given a chattel mortgage or other lien upon his property requiring recording or registering by the State law, and the creditor receiving it might have kept this lien off the record for months or even years thereafter (if not done by collusive agreement) and have filed it within a few days of bankruptcy, and yet the lien would have been held perfectly good, the courts, under these rulings, having declared that the insolvency of the debtor, the existence of a pre-existing debt, and all the other elements of the preference were to be determined as of the date of the transfer between the parties. To be sure, the Amendment of 1903, by declaring the four months period should not begin to run until the date of the recording, where the recording was "required" by state law, evidently attempted to make the date of the recording in such instances the date at which the existence of insolvency, of a pre-existing consideration, of "reasonable cause for belief" and of all the other elements of the preference, should be taken. Nevertheless, that Amendment did not effectually accomplish this object. As the amended law was construed, even if the recording were not done until within the four months period, on the very eve, maybe, of bankruptcy, yet if at the time of the original transfer, which might have occurred a year beforehand, the debtor was solvent, or the lien have been given upon a then presently passing consideration, the transfer was held not to be voidable as a preference, the date of the "transfer" under any theory always being necessarily the date at which all the elements of the preference must be proved to have existed.^{88a}

[Even before Amendment of 1910] In re Sayed, 26 A. B. R. 444, 185 Fed. 962 (D. C. Mich.): "This assignment of the land contract in question was a 'transfer,' and I think the controlling question on this branch of the case must be whether this transfer was 'made' when the paper was signed and delivered and

^{88a}. In re Klein, 28 A. B. R. 263, 197 Fed. 241 (C. C. A. Ohio). This case, In re Klein, the same court sought to distinguish in *Carey v. Donohue*, 31 A. B. R. 210, by saying that the Klein case "did not involve a preference" which is erroneous, as the gist of the Klein action was the recovery of a preference and "preference" was the main point urged, the

chattel mortgage in the Klein case having been kept off the records for eleven months and filed on the eve of bankruptcy, the withholding from record having been made under an arrangement with the bankrupt, he being clearly insolvent at the time of the recording of the deed and the creditor at that time also having had reasonable cause of belief.

took effect as the loans were made, or must be construed as not made until it was recorded. If the former, the transfer was not a preference, because it was not made while the debtor was insolvent, and there was no intent on either side to give or receive a preference, and it was for present and future advances. If the latter, it may be said, owing to the condition of things then existing, to be clearly a preference.

"It is elementary to the definition of a forbidden preference, considered under any section and for any purpose, that it must have been made by the debtor 'while insolvent.' A solvent debtor can not make a preference. It is therefore essential to the argument of the trustee that this transfer of the land contract to the bank was not 'made' in 1907, when it was signed and delivered, nor in 1908, while the bank was making advances on the strength of it; and, indeed, that it had never been 'made' down to the date of the adjudication, because it was not recorded until after adjudication. I can not adopt this theory. This transfer was absolutely and completely made in July, 1907, and all the incidents of security for the amount now due had attached as early as March, 1908, and during all this time Sayed was perfectly solvent, and had a right to give such a security and the bank had a right to receive it.

"Carrying the same inquiry a step further, we find that the intent to give a preference—that is, to pay one creditor leaving other creditors in danger of not being paid as fully—must exist on the part of the giver of the security at the time it is given, and the receiver must then have cause to believe that the giver has such intent. Most certainly, in July, 1907, or March, 1908, Sayed had no such intent, and the bank can not be charged with any notice of an intent which did not exist.

"It is said that a construction of the act which leaves such an unrecorded transfer in legal effect after bankruptcy destroys the force of the act by providing easy means of avoiding the act. If this were true, it could not justify the judicial legislation which seems to me necessary in order to adopt the trustee's theory; but I do not think it is true. The instances where any one has a moral or ethical standing to attack a security given by a perfectly solvent debtor are rare, although they may sometimes occur, and such exceptional instances do not justify straining the statute. If such an instrument is withheld from record by agreement between the parties for the purpose of giving a fictitious credit, it then involves the element of actual fraud, and the question is quite different.

"Some decisions are cited from other circuits, which, while they could be well distinguished on their facts from this case, yet doubtless indicate that the judges writing those opinions thought the statute should be construed as though it said that any transfer, the recording of which was required or permitted by law, should be a preference, if the transferer was insolvent at the time the instrument was recorded; but, in the absence of any controlling decision, I can not accept this view. The intent on the part of the transferer must exist at the critical moment. If that moment be the instant of recording, how can it be said that the transferer then has that intent, when he perhaps gave and delivered the instrument two years before, while he was perfectly solvent, and had continuously supposed that it was recorded, as might well be the case if the lack of recording had been from the carelessness of the secured creditor."

The confusion is to be explained in this way: There are, in reality, two times of transfer in such cases. As between the transferer and transferee, obviously the time of the transfer is the time of the original execution and delivery of the instrument to the grantee or transferee, regardless of its registration; but as to creditors, or the rest of the outer world, the

"transfer" is, by the policy of the State recording statutes, not a complete "transfer" at all until recorded, until delivery to the public recorder—then, and not until then, the debtor signifying to outside parties, to all others who might become interested in his assets, the effectual separation of the lien property from the rest of his assets. This, it must be conceded, is the basic principle upon which rest the recording statutes of the different States. It is also the basic principle of the right to legislate against secret liens. Likewise, in a rightly construed bankruptcy preference statute, the great object should be to make clear that the "transfer," so far as outside parties becoming interested in the estate are concerned, is not complete or perhaps is not even to be considered a "transfer" at all, in cases where State laws require recording as against creditors, until delivery of the instrument to the recorder for registration.^{88b}

In *re Wilson*, 23 A. B. R. 814 (D. C. Hawaii): "There is no requirement in the Hawaiian statutes that bills of sale of chattels must be recorded in order to be valid. The old common law that a bill of sale of chattels was fraudulent and void unless followed by the delivery of the property, is now so modified that continued possession by the vendor only raises a presumption of fraud. Such presumption is removed by registration. The principle of law as found in the rule of the common law and the practice under statutes of registration, appears to be that some kind of public notice is essential in all transfers of property so far as the interests of third parties are concerned. Such notice may be by delivery of the chattels or registry of the bill of sale, or, in the case of transfers of real property, by registration of the conveyance. The transfer of a chose in action or any other property to a creditor is a matter of interest to other creditors, who are likely to be closely watching the course of events in the business of the debtor and who may be prejudiced through ignorance of such a transaction; for instance, through failing to file a petition for adjudication within four months thereafter, where there is insolvency."

Under the decisions, as we have seen in the preceding section, even after the Amendment of 1903, before the Amendment of 1910 creditors were required to prove that, at the time of the "transfer" (that is to say, the transfer between the parties) perhaps several years beforehand, the debtor was then insolvent, which was a practical impossibility, indeed, an unreasonable requirement, since it is always the present insolvent fund of the debtor that is rightly involved and not some ancient fund existing years beforehand.

The Amendment of 1910 makes the date of the recording, where recording is required under State law, the date at which the creditor is to prove the existence of all the elements of a preference—truly the right date, for, as above noted, it is the present insolvent fund with which creditors are concerned, not the debtor's estate in the condition which might have existed several years beforehand.⁸⁹

^{88b}. See Report No. 691 of Senate Judiciary Committee of the 61st Congress, Second Session.

⁸⁹. *Debus v. Yates*, 30 A. B. R. 823, 193 Fed. 427 (D. C. Ky.).

Report No. 691 of Senate Judiciary Committee of the 61st Congress, Second Session.

Obiter [being a conditional sale, it could not be a preference], *In re Farmer's Co. of Barlow* (No. 1), 30 A. B. R. 187, 202 Fed. 1005 (D. C. N. Dak.): "By § 60 (a) of the Bankruptcy Act the contract must be judged as of the date of the filing."

In cases of preferences effected by instruments required to be recorded but which are not recorded at all, the date of the effective "transfer" becomes immaterial as to property in the custody or coming into the custody of the bankruptcy court, since, as to such property, the Amendment of 1910 to Bankr. Act, § 47a (2), gives the trustee the rights of a levying creditor, whereby such lien is avoided without proof of its being a preference. On the other hand, preferences effected by instruments requiring to be recorded but which are not recorded at all, where the property concerned does not come into the custody of the bankruptcy court, must still be proved to have been preferences at the date of the transfer between the parties, except where the State law does not require actual seizure of the property but is satisfied with the existence merely of a creditor holding an execution returned unsatisfied; in which latter event the unrecorded lien, also, may be void by operation of Bankr. Act, § 47 (a) (2), as amended in 1910.⁹⁰

§ 1379 $\frac{3}{4}$. Though Consideration Contemporaneous at Time of Original Transaction Does Failure to Record Make It Preexisting Debt?—The effect of the Amendment of 1910 to § 60b is to bring down to the date of the recording the proof of all the elements requisite to make the transfer a preference. The date of the record, then, is to be considered as the date of the effecting of the "transfer" so far as creditors are concerned. However, it is the transfer that is to be considered as taking place at the date of the recording, not the giving of the original consideration; so that, if the original consideration were contemporaneous with the original transfer between the parties, yet, by virtue of the Amendment of 1910, the date of the transfer is moved forward to the date of the recording, leaving the date of the passing of the original consideration, however, as it stood in the first place.

Compare *Lathrop Bank v. Holland*, 30 A. B. R. 62 (C. C. A. Mo.): "If the bank had taken mortgages as the purchases were made but had refrained from recording them, it could not have prevailed against the trustee in bankruptcy. The oral agreement for a mortgage can give no greater right."

Nevertheless, there is a contrary holding, to the effect that the wording of the statute does not compel such a construction, and that the debt still remains a contemporaneous debt and does not become "pre-existing."⁹¹

§ 1380. Where Recording, etc., Not "Required," Preference Dates from Actual Transfer.—Where the statute does not require reg-

⁹⁰. Compare, phraseology of Bankr. Act, § 60b, as amended in 1910.

⁹¹. That the debt still remains a contemporaneous debt, *In re Watson*, 30 A. B. R. 871, 201 Fed. 962 (D. C. Ky.).

istry or recording, the consummation of the preference will date from the actual transfer, as the State law may determine such date to be.⁹²

§ 1380½. Also Where Instrument Not Recorded, Though Recording "Required."—Likewise, where an instrument is not recorded though recording is "required," the preference dates from the actual transfer between the parties.

In re Watson, 30 A. B. R. 871, 201 Fed. 962 (D. C. Ky.): "In case the transfer has not been recorded, no other time for judging it in those particulars is provided than when it is made."

§ 1381. Whether, Where Not "Required," Preference Dates from Taking of Notorious and Exclusive, etc., Possession.—It is held, in some cases, that where recording or registering is not required by the State law the preference will not even be considered to date from the taking of notorious, exclusive or continuous possession by the beneficiary nor from the giving of actual notice thereof to creditors; and that these provisions of § 3 (b), defining the time limits of a preference as an act of bankruptcy, are not to be imported into § 60 (a) for the recovery of preferences from creditors.⁹³

In re Newton & Co. (Swofford v. Bryant), 18 A. B. R. 567, 153 Fed. 841 (C. A. Ills.): "And further that, under the doctrine obtaining in Arkansas, it would have remained such owner even had an assignee in insolvency of the vendee first secured possession of them. There is no law in Arkansas requiring a contract of conditional sale to be filed or recorded in any public office. Notwithstanding the views which this and other courts have at times entertained as to the effect of an adjudication in bankruptcy, and the right and title of the trustee resulting therefrom, it has been definitely settled by the Supreme Court that the trustee is vested with no better right or title than belonged to the bankrupt; that he stands simply in the shoes of the bankrupt, and as between them he has no greater right. York Mfg. Co. v. Cassell, 201 U. S. 344, 15 Am. B. R. 633. The right of appellant in this case did not first come into existence when it took possession of the property in controversy on the eve of the bankruptcy proceedings. On the contrary, it was secured by the contract which was executed almost a year before, and it is that date which we must regard rather than the date when possession was taken." Quoted further at § 1263.

But other cases hold that the Amendment of 1903 to § 60 was intended

⁹². But compare, *Matthews v. Hardt*, 9 A. B. R. 373, 76 N. Y. Sup. 134; *Laurel Oil Co. v. Horne*, 28 A. B. R. 932 (Sup. Ct. Miss.); *Sturdivant Bank v. Schade*, 27 A. B. R. 673, 195 Fed. 188 (C. C. A. Mo.), reversing 26 A. B. R. 916.

Whether Assignment of Real Estate Mortgage "Required" to Be Recorded.—In re Coffey, 19 A. B. R. 148 (Ref. N. Y.); In re Wilson, 23 A. B. R. 814 (D. C. Hawaii); *Mattley v. Wolfe*, 23 A. B. R. 673, 175 Fed. 619 (D. C. Neb.),

reversed in *Mattley v. Giesler*, 26 A. B. R. 116, 187 Fed. 970 (C. C. A. Neb.), quoted at §§ 1379, 1382½, 1383. Also, see ante, §§ 1139, 1232, 1275, 1334½. This rule is not changed by the Amendment of 1910 to Bankruptcy Act, § 47 (a) (2).

⁹³. *Little v. Hardware Co.*, 13 A. B. R. 422, 133 Fed. 874 (C. C. A. Tex.); In re Wright, 2 A. B. R. 364, 96 Fed. 187 (D. C. Ga.); In re Hunt, 14 A. B. R. 416, 139 Fed. 283 (D. C. N. Y.).

to bring §§ 60 (a) and 3 (a) into harmony in this particular.⁹⁴

Loeser v. Bank & Trust Co., 17 A. B. R. 631, 148 Fed. 975 (C. C. A. Ohio): "What has been the effect of that Amendment? This fact was referred to by Mr. Ray of the House Judiciary Committee, who explained the amendment in question, when proposed in Congress, as intended to prevent preferences under unrecorded instruments given more than four months before the filing of the petition. Touching this he said:

"By adding to 'A' a clause which shall be equivalent to that found in § 3, B, (1). It seems that as § 60a now stands, a preferential mortgage may be given and the creditor preferred, by withholding it from record four months be able to dismiss the trustee suit to recover the same though the paper was actually recorded within the four months period. See *In re Wright* (Ga.), 2 Am. B. R. 364, 96 Fed. 187; *In re Mersman* (N. Y.), 7 Am. B. R. 46.' Vol. 35, part 7, Cong. Record, 6943.

"Before this amendment, § 60a read as follows:

"A person shall be deemed to have given a preference if, being insolvent, he has procured or suffered a judgment to be entered against himself in favor of any person, or made a transfer of any of his property, and the effect of the enforcement of such judgment or transfer will be to enable any one of his creditors to obtain a greater percentage of his debt than any other of such creditors of the same class.' * * *

"(1) A preference which is an act of bankruptcy by § 3 should in an harmonious law be voidable by the trustee. By that section a transfer made by one, 'while insolvent,' of any portion of his property to one or more of his creditors 'with intent to prefer such creditors over his other creditors,' is made an act of bankruptcy, and a petition may be filed against such person 'within four months after the commission of such act.' With respect to the date of the commission of such act of bankruptcy, subdivision (1) of the same section provides, that the date from which the four months begins to run shall be 'the date of the recording or registering of the transfer or assignment when the act consists in having made a transfer of any of his property' * * * 'for the purpose of giving a preference as hereinbefore provided,' * * * 'if by law such recording or registering is required or permitted, or, if it is not, from the date when the beneficiary takes notorious, exclusive or continuous possession of the property unless the petitioning creditors have received actual notice of such transfer or assignment.' By § 60a, a definition of a 'preference' is given which under § 3 would constitute an act of bankruptcy and by § 60b, a 'preference' so defined is made voidable by the trustee. But as we have seen heretofore, § 60a and (b) did not make a preference voidable by the trustee unless the preference, whether under a recorded or unrecorded instrument, was given within four months prior to the filing of a petition in bankruptcy. Thus, a 'preference' under § 3, as denied by § 60a, might constitute an act of bankruptcy and justify an adjudication if given by an unrecorded instrument more than four months prior to bankruptcy and the preference itself be enforced as a perfectly valid act. The plain purpose of the amendment of § 60a was to bring it into harmony with § 3, by making the same period of time the test as to whether a preference may be avoided by the trustee under the former, or may constitute an act of bankruptcy under the latter. The construction given to § 3 should be carried forward and given to § 60a as amended, thus bringing them into consistent relations. 'The two,' said

94. *Long v. Farmers' State Bk.*, 17 A. B. R. 109, 147 Fed. 360 (C. C. A. Iowa); *English v. Ross*, 15 A. B. R. 370, 140 Fed. 630 (D. C. Penn.); *Ragan*

v. Donovan, 26 A. B. R. 311, 189 Fed. 138 (D. C. Ohio), quoted at § 1379; *In re Donnelly*, 27 A. B. R. 504, 193 Fed. 755 (D. C. Ohio).

Judge Archbald, in *English v. Ross*, cited above, 'are intimately related, the one in this particular being the basis of and dominating the other, and it is the failure to realize this and to draw them together as they should be that is responsible for any misapprehension. What is thus "required" in the way of recording in the one is also "required" as a conveyance in the other and for the same purpose.'

"(2) The evil to be corrected was that of secret preferences, given by withholding from record instruments which by the whole policy of recording statutes should be recorded.

"This evil was pointed out by the author of the Amendatory Act of 1903 and the object of the amendment of 60a was stated to be the remedying of this evil. The law as it stood encouraged such secret liens and preferences, for if they could be concealed for four months, though acts of bankruptcy, they were not voidable by the trustee. If we say, that unless the law of the State where the transfer is made makes void all such transfers as to all the world, that it is not a law which 'requires' recording, the evil will continue and judges will continue to bewail the iniquity of a law which makes such a secret transfer an act of bankruptcy and yet holds the preference valid against the bankrupt's estate because made more than four months before starting bankrupt proceedings against the maker. See the lament of Judge Ray, *In re Hunt*, 14 Am. B. R. 416, 139 Fed. 286-287."

In re Reynolds, 18 A. B. R. 666, 153 Fed. 295 (D. C. Ark.); "It was held by the United States Court of Appeals for the Seventh Circuit in *In re Antigo Screen Door Company*, 10 Am. B. R. 306, 123 Fed. 249, that in the absence of fraud such a mortgage is valid under the laws of Wisconsin, as against the trustee under the Bankrupt Act of 1898. An examination of the cases cited in that opinion will show that other courts, notably Massachusetts, have held the same. The evidence does not disclose any fraud when the mortgage was executed as to the property now under discussion, or even that the mortgagor was then insolvent. It was executed for a loan then made. It took nothing away from creditors. The loan was made in good faith, and the mortgagee got possession under it before any liens attached, and before bankruptcy proceedings began, but within four months of the institution of bankruptcy proceedings. I do not find such a mortgage is void as to creditors under the Arkansas decisions, and if not void as to creditors under the Arkansas decisions, it is not invalid under the Bankrupt Act as to the trustee, unless made void by some positive provision of the act. Is the mortgage void, as against the trustee, by any positive provision of the Bankrupt Act? This question, I think, has been answered conclusively by the Eighth Circuit Court of Appeals in the case of *First National Bank of Buchanan County St. Joseph v. Connett*, reported in 15 Am. B. R. 662, 142 Fed. 33. That case is, to all intents and purposes, on all-fours with the case at bar. Indeed, the only difference is that, in that case, the mortgagor was insolvent when the mortgage was given, but the mortgagee was not aware of it. In the case at bar the testimony does not show whether the mortgagor was insolvent when the mortgage was given, or not. But he was insolvent, and the mortgagee knew it, when she took possession. The difference is immaterial, in the opinion of the court; and, therefore, the two cases are on all-fours. * * * The conclusion reached is that the mortgage is void in toto under § 60a of the Bankrupt Act of 1898, as amended by § 13 of the Act of February 5th, 1903. An order will be entered disallowing the claim of Mrs. Poynter in toto until she has surrendered all the property covered by the mortgage in controversy, in her possession or under her con-

trol. Upon a compliance with this order her claim will be allowed as an unsecured claim."

In *re Francis J. Bird*, 25 A. B. R. 24, 180 Fed. 229 (D. C. Minn.): "The important thing is, not that the property be in the possession of the creditor, but that it be out of the possession of the debtor."

And it was held, even before the Amendment of 1903, that § 3 (b) and § 60 (a) should be construed together.⁹⁵

§ 1382. Where "Required" Only as to Bona Fide Purchasers and Encumbrancers or Others Not Creditors.—Where the failure to record or register the transfer does not make the transfer void as to creditors, but only as to bona fide purchasers or encumbrancers, it would seem that the date of the recording would not be the date from which to compute the four months, the case standing precisely as if recording or registering were not required.⁹⁶

Likewise, where the recording or registering is not for the purpose of affecting creditors, but rather to notify debtors or others not creditors, as, for example where the assignment of money under a contract by a public contractor must be filed with the head of the bureau or department in charge of the construction in order to notify the disbursing officer.⁹⁷

However, the rule has been laid down in some well considered cases (discussed in the next section) that if it is "required" for any purpose, as against any person, it is "required" within the purview of Bankr. Act 60 (b) as amended in 1910. Under such ruling, real estate transfers likewise are to be tested for preferences as of the date of the recording, though the recording is only necessary under state law as against bona fide purchasers and encumbrancers.^{97a}

§ 1382½. Or as to Levying Creditors.—One court held that, since "required" refers to creditors, then in states where recording or registering is not "required" in order to be valid against any other creditor than levying creditors the date of the preference is not to be taken as of the date of recording, unless there be such a levying creditor in existence to whose rights the trustee might succeed.⁹⁸ But this case was reversed, the appellate court holding rightly that the word "Required" is descriptive of a general class of instruments with reference to their nature rather than to the particular persons affected by the withholding of it from the records,

⁹⁵. In *re Klingman*, 4 A. B. R. 254, 101 Fed. 691 (D. C. Iowa).

⁹⁶. In *re Sturtevant*, 26 A. B. R. 574, 188 Fed. 196 (C. C. A. Ills.); In *re Hunt*, 14 A. B. R. 416, 139 Fed. 283 (D. C. N. Y.); In *re McIntosh*, 18 A. B. R. 173, 150 Fed. 546 (C. C. A. Calif.). See ante, § 1232.

⁹⁷. *Mattley v. Wolfe*, 23 A. B. R. 673, 175 Fed. 619 (D. C. Neb.), but re-

versed in *Mattley v. Giesler*, 26 A. B. R. 116, 187 Fed. 970 (C. C. A. Neb.).

^{97a}. *Carey v. Donohue*, 31 A. B. R. 210, 209 Fed. 328 (C. C. A. Ohio), quoted at § 1383¾.

⁹⁸. Compare ante, § 1232; also, analogously. In *re Interstate Paving Co.*, 28 A. B. R. 573, 197 Fed. 371 (D. C. N. Y.).

and that it does not require the existence of a levying creditor in any particular case.^{98a}

Mattley v. Giesler, 26 A. B. R. 116, 187 Fed. 970 (C. C. A. Neb., reversing *Mattley v. Wolfe*, 23 A. B. R. 673, 175 Fed. 619): "In *First Nat'l Bank v. Connett* * * * we held that the term 'required' had reference to the character of the instrument of transfer rather than to the particular persons who might or might not be affected by the withholding of it from the records."

Loeser v. Bank & Trust Co., 17 A. B. R. 633, 148 Fed. 475 (C. C. A. Ohio): "We reach the conclusion that the word 'required,' as used in the Amendment, refers to the character of the instrument giving the preference or making the transfer, without reference to the fact that as to certain persons or classes of persons it may be good or bad according to circumstances."

§ 1383. Where State Law Does Not "Require" Recording, but Merely "Permits" It.—Where the State law does not "require" the recording, recording is not necessary, although recording may be "permitted."⁹⁹

Compare, *In re Hunt*, 14 A. B. R. 416, 139 Fed. 283 (D. C. N. Y.): "This last sentence was added by the amendment of February 5, 1903. As introduced in the House of Representatives by the author of the amendment, as it was reported from the Judiciary Committee of the House of Representatives and as it passed the House the words 'or permitted, or if not, from the date when the beneficiary takes notorious, exclusive or continuous possession of the property transferred' followed the word 'required' and ended the sentence. Had the section become a law in this form the ending of the amendment would have been, 'if by law such recording or registering is required or permitted,' etc. In such case there would be no contention here on this subject. In this regard it followed subdivision b, § 3, of the Act. The Senate struck out the words 'or permitted,' etc., above quoted. Did it regard these words as surplusage? Were they surplusage? This court thinks not. The words 'if by law such recording or registering is required' must mean the same as they would if the words 'to make the transfer valid against the person executing it' or 'to make the transfer valid as against the general creditors of the person executing it' were added after the word 'required.' In New York the registering or recording of a mortgage on real estate is not required in order to give it validity as against the mortgagor, or general or even judgment creditors; consequently recording is not required to give it validity as against the trustee in bankruptcy. The word 'required' does not mean the same as 'permitted,' or the same as the words 'required in any case, or for any purpose.' In some States a real estate mortgage must be recorded or registered to be good as against even general creditors. The laws of New York require the recording of such a mortgage as against purchasers and mortgagees in good faith and for value only."

In the case *In re Hunt*, the court—Judge Ray, having himself been the chairman of the Judiciary Committee of the House of Representatives, whose amendment was amended by the striking out of the words "or per-

^{98a}. *Carey v. Donohue*, 31 A. B. R. 210, 209 Fed. 328 (C. C. A. Ohio), quoted at § 1383½.

⁹⁹. See ante, § 1232. Compare, also, *Drug Co. v. Drug Co.*, 14 A. B. R. 477, 136 Fed. 396 (C. C. A. Tex.).

mitted"—held that the word "required" means, not "required in order to make the transfer valid as against creditors" but "required in order to make the transfer valid as against the person executing it" or "as against the general creditors of the person executing it." Notwithstanding the peculiar weight of that court's opinion, arising from the court's intimate acquaintance with the legislation itself, it would seem that the words "or permitted" would not have added to the strength of the Statute nor have made its meaning at all clearer. On the contrary, it would have introduced confusion and uncertainty, for many kinds of transfers are "permitted" to be recorded, if the recorder's fee is paid. Such being the case, the effect of the adoption of the words "or permitted" would have been to make it necessary to record numberless transfers not ordinarily recorded but whose record might be "permitted." Such indeed, is the subsequent criticism of Judge Ray's reasoning by the Circuit Court of Appeals in *Loeser v. Bank & Trust Co.*, 17 A. B. R. 631, 148 Fed. 475 (C. C. A. Ohio), quoted later.

Perhaps the true rule may go even further: that "required" means "*required for any purpose*," that is to say, for validity against levying creditors, general creditors, incumbrancers, transferees, "third persons," or for validity against the bankrupt himself.

First Nat'l Bk. *v. Connett*, 15 A. B. R. 662, 142 Fed. 33 (C. C. A. Mo.): "Within the meaning of amended § 60a of the Bankruptcy Act, the Missouri Law (Rev. St. 1899, § 3404) required the recording of chattel mortgages. To be sure an unrecorded mortgage is not pronounced void absolutely and under all circumstances, but it 'is required to be recorded' in the sense in which that phrase is customarily used, and the language of requirement is similar to that employed in the registry laws of most of the states. The word 'required' found in the phrase 'the recording or registering of the transfer, if by law such recording or registering is required' of the amendment of § 60a, has reference to the character of the instrument of transfer required to be recorded by the State law rather than to the particular individuals who by reason of adventitious circumstances may or may not be affected by an unrecorded instrument. Thus an affirmative answer would unhesitatingly be given to the inquiry: 'Does the law of Missouri require the recording of chattel mortgages?'"

"The Circuit Court of Appeals of the Fifth Circuit, in a case involving the registry statute of Texas, held that, as an unrecorded chattel mortgage was good between the parties thereto and against ordinary creditors, and as there were no intervening lienholders or purchasers, it could not be said that a registry or recording was required, and upon the facts of that case it accordingly concluded that a chattel mortgage given before but placed on record within the four months before the institution of bankruptcy proceedings could not be considered as a voidable preference. *Meyer Bros. Drug Co. v. Pipkin Drug Co.* (C. C. A.), 14 A. B. R. 477, 136 Fed. 396. In effect this is the adoption, without exception or qualification, of the old rule that whether and to what extent a chattel mortgage given before but recorded within the four months period is valid against a trustee in bankruptcy should be determined exclusively by the State law. In our opinion, the Amendment of 1903 has qualified this rule in respect of the question whether such a mortgage may constitute a voidable preference under sub-

divisions 'a' and 'b' of § 60. If this has not resulted, we fail to see that Congress has accomplished anything by the amendment."

Loeser v. Bank & Trust Co., 17 A. B. R. 633, 148 Fed. 475 (C. C. A. Ohio): "Some effect should be given to the amendment of § 60a if the language of the provision will permit. If 'required' be construed as applying only to a law which makes every such transfer absolutely void as to all persons, the amendment will be of no effect, for no recording statute, of which we have any knowledge, makes void transfers or conveyances as between the parties and all of them give effect to such instruments as against some classes of persons having actual notice. The amendment would be idle and the evil sought to be remedied would flourish as before and the legislative purpose be frustrated.

"(4) In view of all of the foregoing considerations we reach the conclusion that the word 'required,' as used in the amendment, refers to the character of the instrument giving the preference or making the transfer, without reference to the fact that as to certain persons or classes of persons it may be good or bad according to circumstances. If to be valid against certain classes of persons, the law of the State 'requires' the constructive notice of registration, it is a transfer which under the amendment is 'required' to be recorded. This takes account of the purpose and policy of recording acts; remedies the evil which flourished under the law before the amendment; gives effect to the plain purpose of Congress; and gives some effect and force to a provision which would otherwise be meaningless, and brings §§ 3 and 60a and 60b into harmony of purpose and meaning.

"(5) We do not ignore the argument, that in § 3 the word 'required' is followed by the words 'or permitted,' and that the latter words are omitted from the amendment, and that the words 'or permitted' were in the Act as introduced by the author of the bill and retained in the amendment as it passed the House but was dropped in the Senate.

"It is a fact of which we may take notice, that it is common to recording statutes to set out a list of contracts, conveyances, and transfers which may be registered, or are 'entitled' or 'permitted' registration. But if an instrument is not 'entitled' or 'permitted' by law to be recorded, its record is of no effect as constructive notice. * * *

"We conclude from the general purpose and policy of recording statutes, that the words 'or permitted' are of no vital signification in § 3. If the instrument giving the preference is one which is 'permitted' to be recorded in order to give it validity as against certain classes of persons, though perfectly valid without record as to other classes, it is an instrument 'required' to be recorded within the meaning of the word as there used. The words 'required' and 'permitted' in the connection used are of synonymous legal meaning. The dropping of the words 'or permitted' by the Senate is, therefore, of vital signification if we are right in regarding § 3 and § 60a as closely connected provisions."

In *re Beckhaus*, 24 A. B. R. 380, 177 Fed. 141 (C. C. A. Ills.): "The last sentence of § 60a 'where the preference, etc.,' was added by the amendment of 1903. As passed by the House the sentence did not end with 'required.' The continuation was 'or permitted, or if it is not, from the date when the beneficiary takes notorious, exclusive, or continuous possession of the property transferred.' These last-quoted words were stricken out by the Senate. Inasmuch as the present case does not involve 'possession,' but turns wholly upon 'recording,' the inquiry is limited to the effect of the excision of the words 'or permitted' after 'required;' and the particular question concerns the soundness of the petitioner's proposition that such excision compels a construction of the amendment as adopted, whereby a chattel mortgage, which a trustee in bankruptcy is assail-

ing as a voidable preference, is not required to be recorded unless an examination of the local law shows that the chattel mortgage, to be impregnable, must be recorded as notice to the persons presently represented by the trustee.

"If, as we are inclined to believe, the Court of Appeals for the Sixth Circuit, in *In re Loeser* (supra), was correct in concluding that 'the words "required" and "permitted" in the connection used are of synonymous legal meaning no effect could be attributed to the dropping of the redundant word.

"If they are not synonymous, the omission of 'permitted' does not imply inevitably (on the basis that no other inference can fairly be drawn) that the law-makers intended that 'required' should be qualified or limited to less than it would have meant if the clause in § 3b and in the original draft of the amendment to § 60a had ended with 'required' for Congress may well have conceived that an insolvent debtor and a diligent creditor were not necessarily to be dealt with in the same way. That is, in the interest of fair and open dealing by those who do business on credit, it might have been thought that an insolvent debtor who does not cause a chattel mortgage given to some of his creditors, to the exclusion of others, to be recorded, whether recording be 'required' or only 'permitted' by the local law, should be liable to be thrown into bankruptcy; while the diligent creditor (diligence being usually favored in the law) should be permitted, after four months, to retain his security, if on taking it he did all the law 'required.' See *Little v. Hardware Co.*, supra.

"Whether the words be deemed synonymous or not, the dropping of 'permitted' only eliminated whatever idea pertained to that word—it could not affect 'required,' for 'required' stands full and untouched, without adverb or clause to cut it down. The primal canon of statutory construction is that the language actually used be given its full and fair meaning, that unqualified words be taken without qualification, and that in the absence of ambiguity extraneous matters be not considered. Under this canon probably nothing more can profitably be said than, if recording is required, it is required. If required for any purpose, or without purpose, how can it be said to be not required? If recording be not required, unless required for all purposes, it could never be said to be required where the instrument is valid between the immediate parties without recording.

"We are further restrained by what seems to us to be the absurd consequences of any other ruling. If a good-faith second mortgage had been taken, then according to the petitioner's theory the trustee could avoid the preference. But if, as is frequently the case, each mortgage was large enough to exhaust the mortgaged property, why should the trustee consume the free assets in his hands in carrying on one end of a lawsuit between the mortgagees? The trustee could gain nothing for the general creditors whichever way the litigation ended, but would be spending their pittances to benefit a preferred creditor. The same would be true even if the recorded second mortgage was less than the value of the mortgaged property; for, on the hypothesis that the trustee has no right to resist the unrecorded first mortgage on behalf of the general creditors, the surplus above the second mortgage would have to be applied upon the first mortgage. Preferential mortgagees and lienholders are 'adverse claimants,' entitled to have their rights determined in plenary suits. They seek to withhold or diminish the fund which otherwise would be shared among the general creditors, and the general creditors are in fact interested in resisting that reduction. Now if the trustee may not assail preferences except in favor of one preferred creditor as against another, and if the general creditors have no interest in such contests except to pray that their fund be not therein completely consumed in costs and fees, the amendment to § 60a not merely failed to accomplish any benefit—it brought about a positive injustice.

"When the amended section is read against the background of the nature and purpose of the act, our interpretation, we believe, is confirmed. The act is a national act. It practically supplants the State insolvency laws. We think it clear that Congress recognized the vast sweep of interstate commerce and meant to free interstate traders from the confusion attendant upon a multiplicity of variant local laws. Therefore the act in all its parts ought to be interpreted in a national view, doing away as far as possible with the variance in the local laws. To release an insolvent debtor from his debts is an act of grace. Through the whole law runs the clear purpose of extending grace only to honest debtors. Honesty, fairness, equity is the whole spirit of the law. Nothing is more abhorrent to equity than deceitful appearances covering secret preferences. So the diligent creditor who obtains security must not help the debtor to be dishonest, unfair, secretive; he can hold his security only on condition that he give his fellow creditors a four-months opportunity to determine whether or not they will file a petition in bankruptcy against the debtor. The openness and fairness of the preferred creditor are made the terms upon which he may retain his preference. In this view the only inquiry is: Does the local law require instruments of the kind in question to be recorded? There is no need of further investigation into the scope or purposes of the local law. There is no concern whether or not the trustee represents innocent purchasers, mortgagees, attachment or execution creditors. No issue is to be made with respect to the validity of the lien claims supposed to be represented by the trustee. Section 60b, which authorizes the trustee to 'recover the property or its value,' says nothing about the representation of the trustee. It is enough on this point that the trustee is the trustee, and that the preferred creditor has failed to record the instrument of transfer, if by the local law instruments of that kind are required for any purpose to be recorded. Only by this interpretation can this national law be administered with anything like uniformity respecting preferences.

"2. Even if the true interpretation of § 60a compelled us to decide this case upon the meaning of the Illinois statute, with due regard to the construction thereof by the Illinois courts, we could not agree with the petitioner.

"Recording a mortgage of chattels left in the possession of the mortgagor is required 'as against the rights and interests of any third person.' The term 'third person' is broad enough to include everybody outside of the immediate parties to the instrument and their privies. A simple contract creditor who has not obtained a judgment is just as much a 'third person,' is just as much a stranger to the mortgage, as is the simple contract creditor who has obtained a judgment. Both have the right to enforce payment, if that can be done. The interests of both are prejudiced if the debtor's property is covered by a fraudulent transfer. If at the time of the fraudulent transfer one creditor has obtained a judgment and the other has not, the only difference is that one has proceeded farther than the other in the enforcement of his rights and the protection of his interests. And when it is said that a fraudulent transfer is void only as to judgment creditors the expression means no more than that a creditor cannot seize his debtor's property until he has obtained some process which authorizes the seizure."

Ragan v. Donovan, 26 A. B. R. 311, 189 Fed. 138 (D. C. Ohio): "And the court proceeds to say (in the Beckhaus case) that any other ruling than that, where recording is required for any purpose or to protect any class of persons, it is 'required' under § 60 (a), is to work positive injustice.

"Chattel mortgages in Illinois, in which State this case was decided, as in Ohio, where the Loeser case was decided, need not be recorded as between the immediate parties, but as to some classes of persons recording is essential to their validity.

"Section 8543, General Code of Ohio (Rev. Stat., § 4134), provides that unrecorded deeds, as to bona fide purchasers for value without knowledge are void; that is to say, for some classes of persons deeds are required to be recorded and as to other classes they are valid without record. Then adopting the reasoning of the Court of Appeals in the Beckhaus case, that, recording being required for some purpose, recording is 'required' under this statute, it seems to us that the application of these authorities to this situation is too clear to need further argument, which might be well grounded upon the case of *English v. Ross*, supra."

[The same rule held to prevail regarding real estate] *Carey v. Donohue*, 31 A. B. R. 210, 209 Fed. 328 (C. C. A. Ohio): "It remains to consider the effect of the four months provisions of §§ 60a and 60b. We look to the deed recording act of the state for the purpose of determining whether, under that act, recording of the instrument under review was required. Concededly this was so as to bona fide purchasers; and the principle is settled in this court that through the operation of § 60 upon a voidable transfer falling within such a state requirement, the trustee may avoid the transfer if registered within the four month's period.

In *re Donnelly*, 27 A. B. R. 509, 193 Fed. 754 (D. C. Ohio): "In the case of *Ragan v. Donovan* (D. C. Ohio), 26 A. B. R. 311, 189 Fed. 138, involving transactions to which the same The Citizens State Banking Company was a party, this court held that the record of a deed is 'required' within the provisions of § 60a of the Bankruptcy Act, providing that a person shall be deemed to have given a preference if, being insolvent, he has within four months before the filing of the petition made a transfer of his property, and that the period of four months within which a petition may be filed alleging the transfer as an act of bankruptcy, if with the intent reprehended by the statute, begins to run from the recording of the transfer.

"We have no reason to doubt the correctness of the holding in that case and the full application of the law as therein stated, if correct, to the situation here."

So that it may, nevertheless, be an instrument of a class "required" to be recorded, within the purview of the Amendments of 1903 and 1910, though the penalty for nonrecord under State law may not be invalidity against everybody nor against all classes of creditors and though no creditor of any class as to whom the unrecorded instrument would be invalid happens to be in existence at the time; for the term "required" describes merely the nature of the instrument.

Mattley v. Giesler, 26 A. B. R. 116, 187 Fed. 970 (C. C. A. Neb.): "It provides that every chattel mortgage not accompanied by immediate delivery and followed by continued change of possession 'shall be absolutely void as against the creditors of the mortgagor, and as against subsequent purchasers and mortgagees in good faith' unless it or a true copy be filed with the county clerk whose duty it is to make certain entries regarding it upon the records of his office. This is a requirement of registration within the meaning of the Bankruptcy Act and it is none the less so though the penalty for noncompliance is not invalidity as to everybody and for all purposes."

§ 1383³/₄. Real Estate Transfers—Date of Recording as Date of Preference.—The rule that the date of the recording is to be referred

to as the date of the preference has been held to be applicable to real estate transfers as much as to transfers of personal property.¹⁰⁰

Carey v. Donohue, 31 A. B. R. 210, 209 Fed. 328 (C. C. A. Ohio): "It remains to consider the effect of the four-months provisions of §§ 60a and 60b. We look to the deed-recording act of the State for the purpose of determining whether under that act recording of the instrument under review was required. Concededly this was so as to bona fide purchasers; and the principle is settled in this court that through the operation of § 60 upon a voidable transfer falling within such a state requirement, the trustee may avoid the transfer if registered within the four-months period. * * * The situation then (in the Loeser Case) evidently demanded of the court an interpretation of the word 'required,' broad enough to embrace all transactions that could displace the rights of the holder of an unregistered chattel mortgage. Anything less than this would have rendered the word 'required' meaningless.

"There can be no difference, then, between the ruling demanded in the Loeser Case and the principle which should govern the instant case. * * * How then can it be that the difference between a deed and a chattel mortgage, as respects form and classes against whom registration is required, amounts to a distinction between this case and the Loeser Case? Further, the form of the present instrument and its inherent infirmities, give to it every attribute that can be ascribed to a 'transfer,' as the term is used in either § 60a or § 60b; and this was true as to that sort of an instrument, even as those sections stood at the date of the Loeser decision. The sections themselves make no distinction respecting the form or the subject-matter of the transfers they condemn; and hence the reason for avoiding such a deed is in every conceivable sense as clear and as strong as can exist in respect of a chattel mortgage."

§ 1384. Preferences as Affected by Taking Possession within Four Months under Unfiled Mortgages or Mortgages Covering After-Acquired Property.—It has previously been observed (ante, § 1236) that unrecorded instruments may be made effective as against the trustee in bankruptcy by the taking of possession thereunder by the mortgagee before the mortgagor's bankruptcy. This will be true even though such possession be taken within the four months prior thereto, if, by the State law, such taking of possession causes the lien to revert to the date of the original transaction, although it is doubtfully true in case the lien is considered by the State law not to so revert but to arise at the date of the taking of possession.

Although "transfers," whether by way of pledge, mortgage, sale, gift or any other or different mode of parting with property, will be preferences under the Bankruptcy Act, if made within the four months preceding the mortgagor's bankruptcy (provided the other elements of a preference co-exist), yet the Bankruptcy Act looks to the State law to determine the time when such "transfer" is held to be consummated, and the facts that constitute a transaction a "sale," or "mortgage" or "pledge," etc. So it is that in States where the taking of possession under an unrecorded instrument

^{100.} [Even before Amendment of R. 311, 189 Fed. 138 (D. C. Ohio), 1910.] Ragan v. Donovan, 26 A. B. quoted at § 1379.

causes the "sale" or "mortgage" or "pledge" to revert to the original date of execution, then in such State the "transfer" will be held to have occurred at the date of the original transaction and not at the date of taking possession.¹

Fisher v. Zollinger, 17 A. B. R. 610, 149 Fed. 54 (C. C. A. Ohio, affirming *In re Nat'l Valve Co.*, 15 A. B. R. 524): "This act of taking possession perfected the lien and made the instrument operative and effective against the world unless the bankrupt trustee has by virtue of some positive provision of the bankrupt law, a right to avoid a mortgage which was good as between the parties and all others who had acquired no intervening rights before the mortgagor took possession. If he has a right to avoid this mortgage under § 60a of the bankrupt law, as a preference made within four months of the filing of the petition in bankruptcy against the mortgagor, it will be because the preference of the mortgage was obtained only when the mortgagee took possession and was not a lien as of the date of the mortgage. But it cannot for a moment be pretended that Zollinger's lien under the mortgage only arose when he took possession. He took possession by virtue of his mortgage and his lien relates to its date. It was not a lien created when he took possession. The lien upon the chattels conveyed was always good as between the parties. That the property was subject to seizure by the process of creditors, or might pass to a subsequent purchaser, may be conceded. The only effect of taking possession was to cut off the possibility of rights accruing to third persons. The status of Zollinger was identical with that of a mortgagee under an unrecorded chattel mortgage. Until recorded the mortgaged property is subject to seizure by third persons. The lien of such an unrecorded mortgage relates to the date of the instrument and is not a preference within the meaning of 60a of the Bankrupt Act, if that date is more than four months antecedent to the filing of a petition in bankruptcy against the mortgagor. *Rogers v. Page*, 15 Am. B. R. 502, 140 Fed. 596; *Humphrey v. Tatman*, 198 U. S. 91, 14 Am. B. R. 74. The effect of the amendment of February 5, 1903, upon such unrecorded instruments we need not here considered. * * *

"But the contention of counsel for appellant is, that it was this act of 'taking possession which created the lien and as this took place on the eve of bankruptcy and at a time when Zollinger knew the National Valve Company was insolvent and could not continue its business,' it was therefore a preference obtained, granted within four months preceding the bankruptcy of that company. The whole case must turn here, for, if the preference claimed by Zollinger is not to be attributed to the mortgage as of its date rather than as of the date of this act of taking possession, the decree of the court below must be reversed in so far as Zollinger was permitted to enforce a lien against such after-acquired property. But we cannot assent to the premise of the argument. The lien of Zollinger against the after-acquired property did not arise when he took possession. As to third persons, at law, it was inchoate. The possession then taken only perfected this incipient lien as against third persons who had not theretofore acquired rights. The question as to whether the lien thus perfected relates to the date of the instrument of mortgages, or to the date when possession was taken, is, in principle, identical with the lien of a mortgage of chattels providing that the mortgagor shall remain in possession with a power of sale, or the lien secured by an unrecorded transfer of property. In both the latter instances

1. See ante, § 1237, et seq.
In re National Valve Co., 15 A. B. R. 524, 140 Fed. 679 (D. C. Ohio, af-

firmed sub nom. *Fisher v. Zollinger*, 7 A. B. R. 618, 149 Fed. 154, C. C. A. Ohio).

the mortgage is a perfectly valid security as between the parties, and voidable only by certain third persons who may acquire rights, in one case before the mortgagee took possession and in the other before the mortgage goes to record. Neither is there anything in the Ohio decisions that will justify any distinction in principle and prevent the lien from relating to the date of the mortgage which included the contract for the lien. It is true that in Ohio, as in some other jurisdictions, the lien upon after-acquired property is not regarded as valid at law until perfected or completed by possession. *Chapman v. Weiman*, 4 Ohio St. 481; *Francisco v. Ryan*, 54 Ohio St. 307. In *Francisco v. Ryan*, the Ohio court, referring to *Chapman v. Weiman*, said:

"The principle upon which that case rests is, that the mortgage constitutes a valid and binding contract between the parties, and being so it must be given effect according to the intention of the parties.' * * * Continuing, the court said of such mortgage: It 'is a complete contract already obligatory upon the parties, and which continues to be so until it is fully executed, so that in taking possession of the acquired property in pursuance of its provisions, the mortgagee exercises a right belonging to him under the mortgage.'

"The court quotes with approval from *Chase v. Denny*, 130 Mass., where it said:

"If the after-acquired property is taken by the mortgagee into his possession before the intervention of any rights of third persons, he holds it under a valid lien by the operation of the provisions of the mortgage in regard to it'.

"Whether the lien of an unrecorded mortgage, or a mortgage of chattels where the mortgagor is left in possession with a power of sale, shall relate to the date of the instrument or to the date when the lien is completed or perfected as against third persons who have acquired no intervening rights before the recording of the instrument or taking possession of the mortgaged chattels, is ordinarily of no importance. All persons are cut off by the recording of the instrument or the taking of possession who have not theretofore acquired some right. This is also true as to the relation of the lien of an after-acquired property clause upon such after-acquired property. It is only when some insolvency statute, or some bankruptcy law, avoiding preferences obtained within a given time before a general assignment or the filing of a petition in bankruptcy is involved, that the date of a preference under such an instrument becomes important. In neither *Chapman v. Weiman* nor *Francisco v. Ryan*, both cited above, was the date of the lien upon the after-acquired property of any importance. Neither was any such question involved in *In re Shirley*, 7 Am. B. R. 299, 112 Fed. 301, or in *In re First National Bank of Canton*, 14 Am. B. R. 180, 135 Fed. 66, and any reference in those cases to the effect of registration as that of a new mortgage was figurative and not intended to intimate that the lien was only of the date of registration. That the lien of an unrecorded mortgage is not of the date of recording but is as of the date of the contract for the lien, is well settled. *Humphrey v. Tatman*, 198 U. S. 91, 14 Am. B. R. 74; *Rogers v. Page et al.*, 15 Am. B. R. 502, 140 Fed. Rep. 342. In case of a mortgage upon property to be acquired, as well as in the other instances above referred to, the lien is the lien contracted for by the instrument of mortgage, and there is just as much room for holding that the lien relates to the date of the contract for the lien in the one instance as in the other. There is nothing in *Francisco v. Ryan* which is antagonistic to this relation of the lien. Upon the contrary, the reasoning of the Ohio court is plainly in line with that of the Vermont court in *Peabody v. Linden*, 61 Vermont 318, and *Thompson v. Fairbanks*, 75 Vermont 361, 369, where it became necessary to decide the date of the lien, because in one case an insolvency statute which avoided preferences obtained within a short time before a general assign-

ment was involved, and the other the effect of § 60a of the Bankrupt Act of 1898 avoiding preferences obtained within four months of bankruptcy."

Some decisions, however, have laid it down as a rule of general law, that the taking of possession under unrecorded instruments within the four months period will not in any event constitute a preference, if the original transaction occurred before the four months;² but those decisions were not rendered recently, and perhaps the Amendment of 1910 to Bankr. Act, § 47 a (2), whereby the trustee is to be deemed vested with all the rights, remedies and powers of a creditor armed with process, as well as the Amendment to Bankr. Act, § 60 (b), above discussed would affect the rule laid down by them.

§ 1384¹₂. Judgments "Within Four Months" but Based upon Attachments Effected before Four Months—Not Preferences.—A preference may be accomplished, as we have seen,³ by way of a judgment or other lien by legal proceedings, but a judgment will not be a preference, of course, unless the depletion of the estate thereby occurred within the four months period; hence a judgment, even though secured within the four months, will not constitute a preference where it is based upon an attachment whose lien was secured before the four months period.⁴

Colston v. Austin Run Mining Co., 28 A. B. R. 92, 194 Fed. 929 (C. C. A. Del.): "Priority is obtained when a lien attaches, and not when it is enforced. The date of the sale is immaterial in this respect; whenever it takes place, it relates back to the date when the lien attached. The attaching creditor in the case before us, therefore, did not obtain a preference by the decree liquidating his debt."

§ 1385. Eighth Element of Preference—Transfer Must Give Creditor Greater Percentage than Other of Same Class.—The effect of the transfer or other appropriation of property must have been to give the creditor receiving it a greater percentage of his claim than some other creditor of the same class in the order of priority. Preference implies advantage of one creditor over others of the same class.⁵

2. *Christ v. Zehner*, 16 A. B. R. 790, 212 Penn. St. 188, 61 Atl. 822, quoting *Sawyer v. Turpin*, 91 U. S. 118.

3. See § 1282.

4. *Crafts-Riordan Shoe Co.*, 26 A. B. R. 449, 185 Fed. 931 (D. C. Mass.). See analogous doctrine, § 1455.

5. See ante, § 128; *West v. Bk. of Lahoma*, 16 A. B. R. 733, 16 Okla. 508; obiter, *In re Bloch*, 15 A. B. R. 750 (C. C. A. N. Y.); impliedly, *Parker v. Black*, 16 A. B. R. 205, 143 Fed. 560 (D. C. N. Y., affirmed in 18 A. B. R. 15); *Spike & Iron Co. v. Allen*, 17 A. B. R. 288 (C. C. A. Va.); *Tumlin v. Bryan*, 21 A. B. R. 319, 165 Fed. 166 (C. C. A. Ga.); *Harder v. Clark*, 23 A. B. R. 756 (City Court of New York);

Mayes v. Palmer, 31 A. B. R. 225, 208 Fed. 97 (C. C. A. Mo.); *Newman v. Dry Goods Co.*, 31 A. B. R. 399 (Kansas City Court of Appeals), quoted §§ 1407 and 1277 note; obiter *Rosenbluth v. DeForest, etc., Co.*, 27 A. B. R. 359 (Sup. Ct. Conn.).

Instance, trust mortgage given to secure ratable claims of all creditors who became such during a certain period, the trustee taking immediate possession of trust property. *Rouse v. Ottenwess & Huxoll*, 31 A. B. R. 115, 208 Fed. 881 (C. C. A. Mich.).

Trivial Transfers.—The court sometimes will disregard an alleged preferential transfer because of its triviality. See ante, § 1279½.

Hart v. Emerson-Brantingham Co., 30 A. B. R. 218, 203 Fed. 60 (D. C. Mo.): "To entitle him to a judgment, it is incumbent upon the plaintiff to both plead and prove that the effect of the transfer complained of was to enable the defendant to obtain a greater percentage of his debt than any [some] other creditor of the bankrupt of the same class. The plaintiff has properly pleaded this essential element of a voidable preference, but no evidence has been submitted to sustain the allegation."

It is obvious that if each creditor receives an equal percentage out of the insolvent fund, there can be no preference—that is precisely the equality that the bankruptcy act itself seeks to bring about. It is only because some one is getting more than his share that the bankruptcy act steps in and prohibits the preference.

Swarts v. Fourth Nat'l Bk., 8 A. B. R. 677, 117 Fed. 1 (C. C. A. Mo.): "The dominant purpose of the prohibition of a preference was not to benefit or injure, or to prevent the benefit or injury, of any creditor or class of creditors, but to prevent the debtor from making any disposition of his property which would prevent its equal distribution—to prevent him from doing anything which would result in the payment out of his property of a larger percentage upon any claim than others of the same class would receive. * * * The test of a preference, under the act, is the payment, out of the bankrupt's property, of a larger percentage of the creditor's claim than other creditors of the same class receive, and not the benefit or injury to the creditor preferred. *Marshall v. Lamb*, 5 Q. B. 115, 126, 127."

Livingston v. Heineman, 10 A. B. R. 41, 120 Fed. 786 (C. C. A. Ohio, reversing, on other grounds, *In re New*, 8 A. B. R. 566): "The equal distribution of the bankrupt's estate among his creditors, contemplated by the Bankruptcy Law, will not admit of one creditor receiving a greater percentage of his debt than any other creditor of the same class."

Obiter, Peterson v. Nash, 7 A. B. R. 181, 112 Fed. 311 (C. C. A. Minn.): "This provision (§ 60 [a]), it seems, does not make the transfer of property (which includes the payment of money), by an insolvent debtor, in and of itself a preference. It must be so done that the effect of the transfer will be to enable one creditor to obtain a greater percentage of his debt than any other creditor of the same class."

In re Denning, 8 A. B. R. 135, 114 Fed. 219 (D. C. Mass.): "Only that is a preference which enables a creditor to obtain a greater percentage of his debt than other creditors of the same class."

Brittain Dry Goods Co. v. Bertenshaw, 11 A. B. R. 629, 68 Kan. 734: "The theory of the national bankrupt law is to secure a distribution of the debtor's property among the creditors ratably and in proportion to their respective claims. If the insolvent debtor himself should make such distribution of his assets, the creditors receiving their equitable shares ought not to be required to restore to the trustee in bankruptcy what they have received, in order that it may be repaid to them again, less the cost of administering the trust. The end and aim of the bankrupt law is to secure payment to creditors of an equal percentage of their claims. If the insolvent person does this, we can see no reason why his creditors should contribute to pay the expenses of bankruptcy proceedings to accomplish the same result."

In re Read, 7 A. B. R. 111 (Ref N. Y.): "Under § 60, subdiv. a, the effect of a preferential transfer must be to enable any one of the bankrupts' creditors to obtain a greater percentage of his debt than any other of such creditors of

the same class. A payment on account which fails to have this effect is not a preference, though all the other elements are present."

Painter v. Napoleon Township, 19 A. B. R. 412, 156 Fed. 289 (D. C. Ohio): "The bill does not aver that the enforcement of the transfer alleged will be to enable the board of trustees to obtain a larger percentage of its debt than any other creditor of the same class. Such an averment is essential to the statement of a cause of action. Section 60a of the Bankrupt Act as amended. 'The test of a preference, under the Act, is the payment, out of the bankrupt's property, of a larger percentage of the creditor's claim than other creditors of the same class receive.' *Swarts v. Fourth Nat. Bank of St. Louis*, 8 Am. B. R. 673, 117 Fed. 1, 4, 54 C. C. A. 387. To recover, the bill must allege and the proof must sustain four statutory elements constituting a preference: 'First, the insolvency of the debtor at the time the judgment was entered or the transfer made in favor of the creditor;' second, that this was done within four months of bankruptcy; third, that the effect of which was that the defendant obtained a greater percentage of his debt than any other creditor of the bankrupt of the same class; and, fourth, that the defendant or his agent had reasonable grounds to believe that it was intended by such transfer of property (or judgment) to give a preference to the defendant within the meaning of the acts of Congress relating to bankruptcy. If the trustee fails to allege any one of these claims, his bill, declaration or petition is bad on demurrer. If he fails to prove all of these elements, judgments should be entered for the defendant.' * * * The bill having failed to allege the third of the foregoing statutory requirements, the demurrer is for this reason sustained."

Thus, deposits in bank, or transfers made to a trustee, with which to pay all creditors of the same class an equal percentage, do not constitute voidable preferences,⁶ although such transfers might be voidable as constituting assignments for the benefit of creditors within four months preceding bankruptcy.

Similarly, where the creditor receiving the transfer assumes all the debtor's other debts and is a responsible party, a preference will not exist.⁷

§ 1386. If No Net Decrease of Indebtedness during Four Months, No Preference.—If there be mutual dealings within the four months, but their result does not decrease the net indebtedness to the creditor, the creditor has not received a greater percentage of his claim than some other creditor of the same class and there is no preference.⁸

§ 1387. Who Are in "Same Class."—The words "the same class" refer to the classes created by the bankruptcy act itself in prescribing the order of priority in the distribution of the general estate among creditors, as, for instance, taxes are in the first class, wages of workmen, clerks and servants are in the second class, other priorities given out of insolvent estates by state or federal laws are in the third class, and all other creditors constitute the fourth and last class. It seems clear that the classes meant

⁶ *Lowell v. International Trust Co.*, 19 A. B. R. 853, 158 Fed. 781 (C. C. A. Mass.).

⁷ *Missouri Elec. Co. v. Hamilton*

Brown Co., 21 A. B. R. 270, 165 Fed. 283 (C. C. A. Mo.), quoted at § 128.

⁸ See ante, "First Element of Preference," § 1296. See post, § 1419.

are precisely the classes created by the Bankruptcy Act itself. The Act, in § 64, prescribes what debts have priority and the order of their priority.

Thus, no preference can be predicated upon the fact that an insolvent debtor has paid his taxes, state, national or municipal, for such taxes constitute a class by themselves entitled to the first place in the order of priority in bankruptcy administration, and no one can blame an insolvent debtor for doing that which the law otherwise would do for him.

Next, no preference can arise from an insolvent debtor paying all of his workmen, clerks and servants in full for their work within three months, even though thereby but a small per cent. is left for other creditors, for workmen, clerks and servants constitute a class by themselves entitled in any event to priority of payment out of the bankrupt estate; so general creditors cannot complain because the debtor paid them in full—it was not at the expense of the general creditors.

Nor do secured creditors constitute such a class, because they are not priority creditors in the true sense of the word—they are not entitled to priority of payment out of the trust funds at all; they own (of course by way of security) a definite and described part of the property in the hands of the trustee that by reason of the ownership does not belong to the trust fund at all;⁹ moreover their rights are not created by any "laws of the States or of the United States" granting priority of payments, so they cannot come within the fifth and last class of priority claimants of § 64; but their rights are created by the voluntary acts of the parties themselves; that is to say, a secured creditor is one who owns, who has the title to, certain definite property which once belonged to the estate and which by this ownership has become separated from the fund out of which, and out of which only, can priority payments be made. Therefore, payment to a secured creditor (unless perchance thereby a corresponding release of property of the debtor is obtained and the property restored to the general fund, as to which, see ante, § 1325) will constitute a preference if it operates to give him a greater percentage of his claim than some unsecured general creditor, for he is not in a separate class by himself but—so far as preferences are concerned—is in the same class with unsecured general creditors; that is to say, neither he nor they are entitled to priority of payment out of the trust fund. Otherwise, as we have seen (ante, § 1325), where there are several secured creditors, holding liens upon the same property, and that property is insufficient to pay them all, the bankrupt could pay out his estate with impunity by paying an equal percentage to each of these secured creditors and, unless the liens were thereby so reduced by the payments as to leave a surplus, there would be nothing for general creditors. It could not be claimed, except as against the last of the secured creditors in the order of priority of liens, that the deficit in the value of the security rendered the claim pro

⁹ In *re Vulcan Foundry & Machine Co.*, 24 A. B. R. 825, 180 Fed. 671 (C. C. A. Pa.), quoted at § 1993.

tanto unsecured, for that reasoning would invalidate only the payment upon the last claim. If, then, a payment to a secured creditor results in releasing a corresponding amount of property to the general creditors, then the payment would not amount to a preference, for it would come under the rule "fair exchange is no robbery." But a payment that would not so operate would be a preference, for general creditors would pro tanto lose part of their so-called trust fund.

The true rule is that the classes meant are the different classes of priority creditors in their order and, lastly, all other creditors.¹⁰

Swarts v. Fourth Nat'l Bk. St. L., 8 A. B. R. 673, 680, 117 Fed. 1 (C. C. A. Mo., reversing *In re Siegel Hillman Dry Goods Co.*, 7 A. B. R. 351): "While it is true that the Bankrupt Act does not define the word 'class,' nor in terms state what creditors are in the same class, it creates some classes, and specifies others, and it seems to us that the meaning of the word 'class' in the act should if possible, be derived from the statute itself. Section 64, after directing the payment of certain expenses of administration, creates three classes of creditors—parties to whom taxes are owing, employees holding claims for certain wages, and those who, by the laws of the States or of the United States, are entitled to priority. Sections 56b, 57e, and 57h provide for the treatment and

10. *Contra*, *In re Proctor*, 6 A. B. R. 660 (Ref. Iowa). *Obiter*, *Mills v. Fisher & Co.*, 20 A. B. R. 237, 159 Fed. 897 (C. C. A. Tenn.); inferentially, *In re Andrews*, 19 A. B. R. 441 (Ref.). Also, *contra*, *In re Kohn*, 2 N. B. N. & R. 367 (note to 7 A. B. R. 111, Ref. Wis.).

But payments made within the four months period to a workman can not be applied upon wages earned before the statutory period, so as to leave a priority claim for the full amount for wages earned within the statutory period; the claimant must surrender his preference on his common claim. *In re King Co.*, 7 A. B. R. 619, 113 Fed. 110 (D. C. Mass.). But, of course, these payments must be shown, since the Amendment of 1903, also to have been received with reasonable cause for belief, etc.

See also, the classifications made in the following cases:

Indorsers held to be in different "class" from holders of unindorsed notes: *In re Happke and Doyle v. Milw. Nat. Bk.*, 8 A. B. R. 535, 116 Fed. 295 (C. C. A. Wis.), where the Circuit Court of Appeals held that the holder of an indorsed note receiving payment in full of it from the indorser but with knowledge or at least reasonable grounds for believing the money came from the bankrupts—the makers—themselves is held to be in a different class from the holder of an unindorsed note.

Landlords held to belong to separate class:

In re Barrett, 6 A. B. R. 199 (Ref. N. Y.), wherein a landlord was held to belong to a class by himself. This decision was right in its results but not for the reasons stated in the opinion. The proper reason was that the payment of current rent is not the payment of a pre-existing debt but is based upon a contemporaneously arising consideration.

In re Belknap, 12 A. B. R. 326 (D. C. Penn.). Also, see *obiter* in *Livingston v. Heineman*, 10 A. B. R. 39, 120 Fed. 786 (C. C. A. Ohio), where the Circuit Court of Appeals divides the creditors into two classes, to be sure, making priority creditors one class but confining the second class to unsecured or general creditors.

Joint and separate creditors of partnership and individual partners held not to belong to same class: *Obiter*, *In re Denning*, 8 A. B. R. 136, 114 Fed. 801 (D. C. Mass.).

Wife held to belong to separate class as regards repayment to her of dowry by bankrupt husband in Louisiana, within the four months preceding bankruptcy of the husband. *Gomila v. Wilcombe*, 18 A. B. R. 143, 151 Fed. 470 (C. C. A. La.).

Creditor Receiving Security Given for Present Loan Held Not to Be in Same Class with Existing Creditor.—*In re Sayed*, 26 A. B. R. 444, 185 Fed. 962 (D. C. Mich.).

disposition of claims secured by property, and of claims which have priority. The creditors who hold these various claims, and the general creditors of the estate, constitute the classes of creditors of which the Bankrupt Act treats. Now, if any one of these various classes is taken by itself and examined, it will be seen that each of the creditors in the same class always receives the same percentage upon his claim, out of the estate of the bankrupt, that every other creditor of his class receives. Where the estate is insufficient to pay the claims of different classes in full, the classes receive, out of the bankrupt estate, different percentages of their claims, but creditors of the same class receive the same percentage. The test of classification is the percentage paid upon the claims out of the estate of the bankrupt."

Livingston v. Heineman, 10 A. B. R. 42, 120 Fed. 786 (C. C. A. Ohio, reversing, on other grounds, *In re New*, 8 A. B. R. 566): " * * * and there are two general classes—first, those who have priority and are to be paid in full; and, second, general or unsecured creditors, among whom the balance remaining after paying the creditors of the first class, is to be distributed equally, in proportion to the amount of their respective claims."

Inferentially, *In re Read*, 7 A. B. R. 111 (Ref. N. Y.): "Workmen, clerks, and servants constitute a distinct class of creditors, and certain conditions and privileges are attached to their claims. If, therefore, there are sufficient assets to pay all workmen, clerks or servants of the same class in full, payments on account prior to the bankruptcy are immaterial, as each creditor of that class is fully paid, and therefore there can be no preference of one over another. It would be circuitous remedy, if creditors so situated should be compelled to refund a preference and then immediately have it returned to them."

In re Belknap, 12 A. B. R. 326 (D. C. Penna.): In this case the court held that a landlord entitled to priority out of insolvent funds by State law is not in the "same class" with unsecured creditors, the court saying: "There is no other creditor of the same class, for there is but a single landlord; and, as the claim for rent had priority over the claims of the general creditors, the distress did not enable the landlord to obtain a greater percentage of his debt. The rent was entitled to be paid first out of the proceeds of the very property upon which the distress was levied, whenever it should be sold by the trustee, and therefore the distress gave no new light, but merely hastened the time of payment. When he distrains, a landlord is simply enforcing the priority which is given to him by law, and in no way gains any improper advantage over other creditors by thus converting the property into money more speedily."

In re Feuerlicht, 8 A. B. R. 550 (Ref. N. Y.): "It seems to me that the motion of the trustee in this matter cannot be allowed for the reason that this is a preferred (priority) claim, and even if a payment to a servant of a part of his wages could be called a preference, in this matter the result would simply be that the claimant would be obliged to pay back to the trustee in bankruptcy, the amount that he has received on account and then demand from the trustee as a preference for wages, the whole of the amount of his wages."

In re Flick, 5 A. B. R. 465, 105 Fed. 503 (Ref. Ohio): "A preference to a person entitled to a priority would only be considered a preference as to other creditors entitled to the same priority and not as to general creditors."

§ 1387½. Firm and Individual Creditors Belong to Different Classes.—Firm and individual creditors belong to different classes; for they each have certain rights reciprocally in the other's estate; so that, in due order of priority, firm creditors are also creditors of each individual and vice versa. Thus it is that an individual transfer to pay a firm debt

may constitute individual preference, if other firm creditors (the "same class") do not get a like transfer.¹¹

§ 1388. **Preferences among Priority Creditors.**—Of course even in the case of payments to those entitled to priority as for instance, a workman, a preference would exist if the insolvent had paid one workman a greater percentage of his claim than the others would receive out of the estate.¹²

§ 1389. **Actual Receipt of Like Percentage by Other Creditors Not Essential to Exoneration from Charge of Preference, if Enough Left.**—It is not necessary that other creditors of the same class actually shall have received the same proportion in order to exonerate from the charge of preference, if enough is left to give them the same proportion.¹³

Brittain Dry Goods Co. v. Bertenshaw, 11 A. B. R. 631, 68 Kas. 734: "There was a finding that the payment to defendant below prevented the remaining creditors from securing payment of their claims from Ridgeway & Co., but, in the light of other answers of the jury, this means that the payment had the effect to prevent a payment in full to other creditors. In the case of *Pepperdine v. Bank* * * * the principle was recognized that if the debtor making the payment had paid, or made provision to pay, other creditors a proportionate amount, the transaction was not a preference. It is essential to a recovery in cases of this kind that the effect of the payment was to enable one creditor to obtain a greater percentage of his debt than other creditors of the same class."

§ 1390. **Modes of Proving This Element.**—It has been held that proof of its being a preference over others may be established by showing that some other creditors of the same class had received nothing on account during the same period.¹⁴

In *re Mayo Contracting Co.*, 19 A. B. R. 551, 157 Fed. 469 (D. C. Mass.): "If there is any other creditor of the same class who, by the enforcement of the transfer in question, will obtain a less percentage of his debt than the petitioner, I think that the transfer was a preference under § 60 (a) of the Bankruptcy Act, and that it was none the less a preference, even though it be true that some creditors can be found who have received larger percentages through other payments made to them within the four months."

Compare, *obiter*, *Hart v. Emmerson-Brantingham*, 30 A. B. R. 218, 203 Fed. 60 (D. C. Mo.): "The evidence fails to show what assets came into the hands of the trustee, and what creditors are entitled to participate in the distribution, and hence it is impossible to determine whether the return of the defendant's goods has resulted in giving it a greater percentage of its debt than has, or will be, paid to other creditors."

Or by showing that the creditor receiving the transfer received full pay

11. Upon this subject, see the full discussions of §§ 171, 1291, 1303¼, 1312¼, 1312½, 2268½. Also, compare, *obiter*, In *re Denning*, 8 A. B. R. 136, 114 Fed. 801 (D. C. Mass.).

12. Inferentially, In *re Read*, 7 A. B. R. 111 (Ref. N. Y.); inferentially, *obiter*, In *re Flick*, 5 A. B. R. 465, 105 Fed. 503 (Ref. Ohio).

Government Contracts, Sureties Paying on.—See post, § 2191.

13. Inferentially, *Brittain Dry Goods Co. v. Bertenshaw*, 11 A. B. R. 631, 68 Kas. 734; *Pepperdine v. Bank*, 10 A. B. R. 570, 84 Mo. App. 234, 242.

14. In *re Colton Export and Import Co.*, 10 A. B. R. 14, 121 Fed. 663 (C. C. A. N. Y.).

or full security, while not sufficient was left to pay or secure all remaining creditors in full.¹⁵

Coder v. McPherson, 18 A. B. R. 523, 152 Fed. 951 (C. C. A. Iowa): "As Armstrong was insolvent when he gave the mortgages, their necessary effect was to enable one of his creditors to obtain a greater percentage of its debt than others of the same class, and they therefore created a preference under § 60a."

Or that the transfer was of all his property not exempt from execution, leaving other creditors unpaid.

Gering v. Leyda, 26 A. B. R. 137, 186 Fed. 110 (C. C. A. Neb.): "The evidence submitted in the trial court warranted the jury in concluding that the transfer of the stock of goods and open accounts to plaintiffs in error would enable them to obtain a greater percentage of their debts than other creditors of bankrupt of the same class. The evidence showed that at the time of the sale of the stock and accounts to plaintiffs in error, the bankrupt was indebted to various other creditors whose claims were unsecured and the evidence tended to show that besides the stock of merchandise and accounts, the bankrupt owned no other property that was not exempt from execution."

Obiter, Brittain Dry Goods Co. v. Bertenshaw, 11 A. B. R. 631, 68 Kas. 734: "If plaintiffs in error had received all of their claim, the payment manifestly would have been a preference, for it was clearly shown that the debtor's assets were insufficient to satisfy all they owed."

Of course, unless the debtor were insolvent the transfer could not operate to give the creditor a greater percentage.

McDonald v. Clearwater R. Co., 21 A. B. R. 182, 164 Fed. 1007 (C. C. Idaho): "Not only is there no proof of the aggregate of the lumber company's property at a fair valuation upon the date of the assignment, but the record is also silent as to the value of the bankrupt's assets at any time after the bankruptcy proceedings were instituted. That being the case, upon what basis can the court make a finding that the effect of the assignment was to enable the bank to obtain a greater percentage of its debt than other creditors of the same class?"

§ 1391. Transfer Not Necessarily to Creditor nor Agent if Benefit Accrues to Creditor.—The transfer need not be to the creditor nor to his agent, so long as the effect of it is to enable the creditor to receive out of the debtor's estate a larger percentage of his claim than others of the same class.¹⁶

§ 1392. But Either Actual Receipt or Actual Benefit Requisite.—The property must have been actually received by the creditor or the creditor have actually gotten the benefit of it in some way.¹⁷

15. *Crooks v. People's Nat'l Bk.*, 3 A. B. R. 238, 46 App. Div. (N. Y.) 335 (N. Y. Sup. Ct. App.).

Still another instance, *Swarts v. Fourth Nat'l Bk.*, 8 A. B. R. 673, 117 Fed. 1 (C. C. A. Mo.): Two debts upon promissory notes; one series of notes had two accommodation indorsers: the other had four accommodation endorsers: preferences were received on one series of notes; held the

preferences must be surrendered before either claim can be allowed, for the two series of notes were in the same "class."

16. See ante, §§ 1300, 1301, 1301½, et seq.

17. Instance where not received nor benefit had: Agent himself a creditor receiving a preference, the surplus to be turned over to principal, who was also a creditor—no surplus shown to

Creditors actually receiving the fruits of a preference also are bound, although not authorizing the proceeding.¹⁸

§ 1393. Resume.—In explicating the subject of preferences, the eight elements have now been considered which constitute a preference under the present Bankruptcy Act. To recount: Preference implies:

First, *an appropriation of property and depletion of the trust fund*: some portion of the debtor's property must have been appropriated by the transaction to the payment of a claim;

Implies, second, *an application of the property to the benefit of a creditor*: The claim upon which the preferential transfer is made must have been the claim of a creditor;

Implies, third, *a preceding creditor*: The creditor's claim must have been a debt—a pre-existing debt;

Implies, fourth, *voluntary action of the debtor*: The debtor must have made a "transfer" or have "procured" or "suffered" the creditor to obtain a judgment, whose enforcement would have operated to appropriate property of the debtor;

Implies, fifth, *an application of the property upon a debt*.

Implies, sixth, *insolvency of the debtor*: The debtor must have been insolvent at the time of the transfer or other appropriation of property;

Implies, seventh, *a transaction or recording within the four months preceding bankruptcy*: The transfer or other appropriation of property, or at any rate the recording of it where recording is required by law, must have been made within four months before the filing of the bankruptcy petition;

Implies, eighth, *an advantage to be acquired by one creditor over others of the same class*: The effect of the transfer or other appropriation of property in the event it were undisturbed must have been to give the creditor receiving it a greater percentage of his claim than some other creditor of the same class.

With any of these elements lacking there is no preference; with them all existing a preference exists.¹⁹

Thus, mere knowledge of a debtor's insolvency cannot transform into a preference an act which otherwise is no preference.

In re King Co., 7 A. B. R. 619, 113 Fed. 110 (D. C. Mass.): "Bankrupt Act, § 60b, does not provide that the trustee may recover all payments received with knowledge of insolvency, but only preferences so received. This seems to be the inevitable result of Dickson v. Wyman, combined with Pirie v. Trust Co. I must hold, therefore, that knowledge of insolvency did not make a preference of acts which otherwise did not amount to a preference."

exist, In re Hickey, 7 A. B. R. 282 (D. C. Iowa): A transfer of book accounts.

18. Stern, Falk & Co. v. Trust Co., 7 A. B. R. 305, 112 Fed. 501 (C. C. A. Ky.).

19. Eventual Adjudication of Bank-

ruptcy, Also Necessary Element.—Of course eventual adjudication of the debtor as a bankrupt is also implied, for the special rights conferred by the bankruptcy law in regard to preferences are dependent on the debtor being adjudged bankrupt.

§ **1394. Voidable Preferences.**—Now, while proof of these eight elements will establish a preference, yet, without proof of other elements, they fall short of having any practical effect, either as establishing an act of bankruptcy or a recoverable preference.²⁰

Unless proof also be made that the debtor made the transfer, or procured the judgment to be taken with intent to prefer the creditor receiving it, the proof will fall short of a preference amounting to an act of bankruptcy. Again, unless it is proved that the creditor receiving it, or his agent acting therein, had reasonable cause to believe the transfer would effect a preference then it also falls short of being proof of a voidable preference and the creditor will not be obliged to surrender the property so received by him.

Thus a preference itself has eight elements, as above noted; a preference that amounts to an act of bankruptcy as also noted has these same eight elements and one more element, namely, the debtor's intent to prefer, making nine elements in all; whilst a preference that is voidable so that the property affected by it can be recovered again for the benefit of the bankrupt estate, has the same eight elements, and also one additional element, although this additional element is not the identical additional element requisite to make the preference an act of bankruptcy.

Compare, *In re Kerlin*, 31 A. B. R. 12, — Fed. — (C. C. A. Ohio, reversing S. C., 30 A. B. R. 816, — Fed. —) "Distinction is urged between the preference defined by that section [§ 60] and the preference forbidden by § 3, art. 2. The difference between a transfer 'with intent to prefer' which is made an act of bankruptcy by the latter provision, and the 'preference' denounced by the former, even since the amendment of 1910, § 60 b, is, as respects the present issue, formal rather than material. True 'intent to prefer,' within the meaning of § 3, art. 2, relates to the debtor, while 'reasonable cause to believe' under § 60 b refers to the creditor; but this difference can affect only the evidence calculated to reveal the debtor's intent in the one instance and the creditor's belief in the other; for there is complete identity between the object of a preference made under the one and that received under the other."

§ **1395. Ninth Additional Element Requisite to Make Preference Voidable—Creditor Must Have Had "Reasonable Cause to Believe" Preference "Would Be Effected."**—The additional element requisite to make a preference voidable is that the creditor (or his agent) receiving the preference must have received it under such circumstances as naturally would have caused the ordinary person, had he

²⁰. See note to *Crooks v. People's Nat'l Bk.*, 3 A. B. R. 238. See note to *In re McLam*, 3 A. B. R. 246, 248 (D. C. Vt.).

Effect of Amendment of 1903 in the Particular of "Reasonable Cause of Belief."—*In re Tindal*, 18 A. B. R. 773, 155 Fed. 456 (D. C. S. Car.): "The main object of the Bankrupt Act and one of its most beneficial results, was

an equal distribution among his creditors of the estate of the bankrupt. The effect of the amendment referred to is in most cases to practically defeat this beneficial intent, for it becomes necessary now to prove that the party receiving the preference had reasonable cause to believe that it was intended thereby to give the preference."

been the creditor receiving the preference, to have believed that thereby a preference would be effected.²¹

21. Bankr. Act, § 60 (b) as amended in 1919: "If a bankrupt shall have procured or suffered a judgment to be entered against him in favor of any person or have made a transfer of any of his property, and if, at the time of the transfer, or of the entry of the judgment, or of the recording or registering of the transfer if by law recording or registration thereof is required, and being within four months before the filing of the petition in bankruptcy or after the filing thereof and before the adjudication, the bankrupt be insolvent and the judgment or transfer then operate as a preference, and the person receiving it or to be benefited thereby, or his agent acting therein, shall then have reasonable cause to believe that the enforcement of such judgment or transfer would effect a preference, it shall be voidable by the trustee and he may recover the property or its value from such person." In re Banks, 31 A. B. R. 270, 207 Fed. 662 (D. C. N. Y.); In re Carlile, 29 A. B. R. 373, 199 Fed. 612 (D. C. N. Car.).

[Concurring opinion] Aiello v. Crampton, 29 A. B. R. 1, 201 Fed. 891 (C. C. A. N. Mex.), but this case though decided since the Amendment of 1910 to Bankr. Act, § 60 (b), nevertheless reverts to the old law and holds that there was insufficient evidence that the bankrupt "intended" a preference.

[Though arising after the Amendment of 1910 to § 60 (b) the court proceeds on assumption of old law]. In re Varley, etc., Co., 26 A. B. R. 840, 188 Fed. 761 (D. C. Ala.).

Cases Arising before Amendment of 1910.—*Crooks v. Peoples' Bk.*, 3 A. B. R. 243, 46 App. Div. (N. Y.) 335; *Baden v. Bertenshaw*, 11 A. B. R. 308, 68 Kans. 32; *Hicks v. Langhorst*, 6 A. B. R. 178 (Ohio Com. Pleas); *Sav. Bk. v. Jewelry Co.*, 12 A. B. R. 781, 123 Iowa 432; *Keith v. Gettysburg Nat'l Bk.*, 10 A. B. R. 762, 23 Penn. Superior Court 14; *Babbitt v. Kelly*, 9 A. B. R. 338, 70 S. W. 384 (Mo. Ct. App.); *Deland v. Miller*, 11 A. B. R. 744, 119 Iowa 368; *Upson v. Mt. Morris Bk.*, 14 A. B. R. 6 (N. Y. Sup. Ct. App. Div.); *Laundy v. Nat'l Bk.*, 11 A. B. R. 223 (Kans. Sup. Ct.); In re Clifford, 14 A. B. R. 281, 136 Fed. 475 (D. C. Iowa); *Benedict v. Deshell*, 11 A. B. R. 20, 177 N. Y. 1, 68 N. E. 999; *Hussey*

v. Dry Goods Co., 17 A. B. R. 513, 148 Fed. 598 (C. C. A. Kans.); In re Bartheleme, 11 A. B. R. 70 (Ref. N. Y.); *Sebring v. Wellington*, 6 A. B. R. 673 (N. Y. Sup. Ct. App. Div.); In re Eggert, 4 A. B. R. 456, 102 Fed. 735 (C. C. A. Wis., affirming 3 A. B. R. 541); In re Armstrong, 16 A. B. R. 583, 145 Fed. 202 (D. C. Iowa); *Critenden v. Barton*, 5 A. B. R. 775 (N. Y. Sup. Ct. App. Div.); In re Hines, 16 A. B. R. 495, 144 Fed. 543 (D. C. Penn.); impliedly, *Kaufman v. Treadway*, 12 A. B. R. 684, 195 U. S. 271; impliedly, *Hackney v. Hargreaves Bros.*, 13 A. B. R. 164, 68 Neb. 634; impliedly, *Turner v. Fisher*, 13 A. B. R. 243, 133 Fed. 594 (D. C. Calif.); impliedly, *Brown v. Guichard*, 7 A. B. R. 518 (Sup. Ct. N. Y.); impliedly, *Sundheim v. Ridge Ave. Bk.*, 15 A. B. R. 134, 138 Fed. 951 (D. C. Pa.); impliedly, *Wetstein v. Franciscus*, 13 A. B. R. 326, 133 Fed. 900 (C. C. A. N. Y.). See note to In re Jacobs, 1 A. B. R. 518 (D. C. La.). Impliedly, *English v. Ross*, 15 A. B. R. 373, 140 Fed. 630 (D. C. Iowa); impliedly, *Crandall v. Coats*, 13 A. B. R. 712, 133 Fed. 965 (D. C. Iowa); impliedly, In re Andrews, 14 A. B. R. 247, 135 Fed. 599 (D. C. Mass.); impliedly, *Thomas v. Adelman*, 14 A. B. R. 511, 136 Fed. 973 (D. C. N. Y.); In re Goodhile, 12 A. B. R. 374, 130 Fed. 782 (D. C. Iowa); impliedly, *Stedman v. Bk.*, 9 A. B. R. 7, 117 Fed. 237 (C. C. A. Iowa); impliedly, In re Virginia Hardwood Mfg. Co., 15 A. B. R. 136, 139 Fed. 209 (D. C. Ark.); impliedly, In re Beerman, 7 A. B. R. 431, 112 Fed. 663 (D. C. Ga.); impliedly, *Bank v. Sundheim*, 16 A. B. R. 863 (C. C. A. Penn.); impliedly, *Plate Glass Co. v. Edwards*, 17 A. B. R. 447 (C. C. A. Iowa).

It is held in one case that decisions under the law of 1867, are applicable: *Stevenson v. Milliken*, 13 A. B. R. 206, 99 Me. 320. But it is denied in another case that such decisions are applicable, In re Andrews, 16 A. B. R. 387 (C. C. A. Mass.).

Further cases arising before Amendment of 1910: *Brewster v. Golf Lumber Co.*, 21 A. B. R. 106, 164 Fed. 124 (D. C. Pa.), quoted at § 1410; *Curtiss v. Kingman*, 20 A. B. R. 95, 159 Fed. 880 (C. C. A. Mass.); In re Tindal, 18 A. B. R. 773, 155 Fed. 456 (D. C. S. Car.), quoted at § 1394, note; In re Pfaffinger, 18 A. B. R. 807, 154 Fed. 528 (D. C. Ky.), quoted at

A voidable preference implies intent or willingness on the creditor's part to deplete the insolvent fund in order to obtain satisfaction in whole or in part of his own claim.

Carey v. Donohue, 31 A. B. R. 219, 209 Fed. 328 (C. C. A. Ohio): "It is true, as counsel claim, that this court has held that in a suit to set aside a voidable preference, it is necessary to allege that the person receiving the preference had reason to believe that it was intended to give 'a preference forbidden by law.' In re Leech, 22 A. B. R. 599, 171 Fed. 625. While that decision was rendered

§ 1399; Rutland County Natl. Bk. v. Graves, 19 A. B. R. 446, 156 Fed. 168 (D. C. Vt.); Tumlin v. Bryan, 21 A. B. R. 319, 165 Fed. 166 (C. C. A. Ga.); In re Lynn Camp Coal Co., 22 A. B. R. 60, 168 Fed. 998 (D. C. Ky.); In re Neill-Pinckney-Maxwell Co., 22 A. B. R. 401, 170 Fed. 481 (D. C. Pa.); In re Burlage Bros., 22 A. B. R. 410, 169 Fed. 1006 (D. C. Iowa); In re Leech, 22 A. B. R. 599, 171 Fed. 622 (C. C. A. Ky.); Taylor, trustee, v. Nichols, 23 A. B. R. 310, 134 App. Div. (N. Y.) 787; In re Wolf Co., 21 A. B. R. 73, 164 Fed. 448 (D. C. Pa.); In re Kulberg, 23 A. B. R. 758, 176 Fed. 585 (D. C. Minn.); In re Bartlett, 22 A. B. R. 891, 172 Fed. 679 (D. C. Pa.); Whitwell, Trustee, v. Wright, 23 A. B. R. 747, 136 A. D. N. Y. 246; In re Peacock, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.).

Stern v. Paper, 25 A. B. R. 451, 183 Fed. 228 (D. C. N. D.): "'Reasonable cause to believe under Section 60 of the Bankruptcy Act, covers substantially the same field as 'notice' in determining whether a person is a bona fide purchaser of property. Hence, under this statute 'notice of facts which would incite a person of reasonable prudence to an inquiry under similar circumstances is notice of all the facts which a reasonably diligent inquiry would develop.' Coder v. McPheson (C. C. A.), 18 A. B. R. 523, 152 Fed. 951."

Instance, claim placed in attorney's hands. In re Thomas Deutschle & Co. (No. 2), 25 A. B. R. 348, 182 Fed. 435 (D. C. Pa.); instance, stopping in transitu, In re Thomas Deutschle & Co. (No. 2), 25 A. B. R. 348, 182 Fed. 435 (D. C. Pa.).

Powell v. Gate City Bank, 24 A. B. R. 317, 178 Fed. 610 (C. C. A. Mo.): "Although the payment to the bank effected a preference it was not voidable unless the bank had reasonable cause to believe that it was intended to give it a preference thereby [now "to believe that a preference would be effected thereby"].

Hamilton Nat. Bank v. Balcombe, 24 A. B. R. 338, 177 Fed. 155 (C. C. A. Ills.); Sparks v. Marsh, 24 A. B. R.

280, 177 Fed. 739 (D. C. Ark.); Reber v. Louis Shulman & Bro., 25 A. B. R. 475, 183 Fed. 564 (C. C. A. Pa.), affirming 24 A. B. R. 782; Ommen v. Talcott, 26 A. B. R. 689, 188 Fed. 401 (C. C. A. N. Y.); Kimmerle v. Farr, 26 A. B. R. 818, 189 Fed. 294 (C. C. A. Mich.); Boswell Nat. Bank v. Simmons, 26 A. B. R. 865, 190 Fed. 735 (C. C. A. Okla.); Dougherty v. First Nat. Bank, 28 A. B. R. 263, 197 Fed. 241 (C. C. A. Ohio); Fowler State Bank v. White, 28 A. B. R. 441, 198 Fed. 631 (C. C. A. Kan.); Stanley v. Pajaro Valley Bank, 28 A. B. R. 467, 196 Fed. 365 (C. C. A. Cal.); Templeton v. Wollens, 29 A. B. R. 208, 200 Fed. 257 (C. C. A. N. Y.).

Cullinane v. State Bk. of Waverly, 12 A. B. R. 779, 123 Iowa 340: "A finding that such was the fact—conceding insolvency—would not be sufficient of itself to defeat the lien of the mortgage. The bank must have had reasonable cause to believe not only that insolvency existed as a fact, but that a preference was intended; and this must be made to appear before the mortgage can be avoided at the suit of the trustee. This is the express provision of the Bankruptcy Act."

Levor v. Seiter, 8 A. B. R. 459 (N. Y. Sup. Ct. App. Div.): "The allegations of the complaint may be sufficient as setting forth a cause of action under § 60 of the Bankruptcy Law, but the proof failed to disclose the existence of an element necessary to the maintenance of an action under that section, namely, that the defendants had reasonable cause to believe that their debtors, by suffering a judgment to be taken against them, intended to give a preference to the defendants."

Johnson v. Anderson, 11 A. B. R. 294 (Sup. Ct. Neb.): "The trustee in bankruptcy may recover money paid by the bankrupt as a preference only when the person receiving it had reasonable ground to believe a preference was intended."

Compare, In re Eggert, 4 A. B. R. 452, 107 Fed. 735 (C. C. A. Wis.): "While, therefore, rulings under the former act are inapplicable, in a cer-

before, and the present transaction occurred since, the amendment of 1910 to § 60b, yet the element of reasonable belief of the creditor remains as a fact necessary in substance to allege."

In *re Herman*, 31 A. B. R. 243, 207 Fed. 594 (D. C. Iowa): "Under the section as so amended [§ 60 (b) amended June 25, 1910] if the bankrupt be in fact insolvent, it is only necessary that the person receiving the transfer, or his or her agent acting therein, shall have reasonable cause to believe that the enforcement of such transfer will effect a preference to render the transfer voidable by the trustee. See *Alexander v. Redmond* (C. C. A.), 24 A. B. R. 620, 180 Fed. 95, where it was so held by the court of appeals, 2nd circuit prior to this amendment."

Rogers v. American Halibut Co., 31 A. B. R. 576 (Mass.): "The intention of the bankrupt to confer a preference no longer need be shown, but the plaintiff under the statute as amended still has the burden of proving that the defendant when the payment was received had reasonable cause to believe its debtor was insolvent and that the enforcement of the transfer would result in diminishing the bankrupt's assets applicable for the payment of creditors of the same class."

Ogden v. Reddich, 29 A. B. R. 531, 200 Fed. 977 (D. C. Ky.): "Reasonable cause to believe that the mortgage would effect a preference was reasonable cause to believe that it would operate as a preference. Effect a preference and operate as a preference I understand to be the same thing. The requirement in terms is not that mortgagee or his agent should have reasonable cause to believe that the bankrupt was insolvent and the mortgage would effect a preference, but only that it should have reasonable cause to believe that the mortgage would effect a preference. Belief that the mortgage would effect a preference—i. e., that the property covered thereby was a greater percentage of the bankrupt's property than on a distribution thereof amongst his creditors would be received by his other creditors of the same class—necessarily involved belief that the bankrupt was insolvent, for not otherwise could the mortgagee have had such belief."

"The requirement, therefore, is not only that the bankrupt was insolvent and that the mortgage covered such greater percentage of his property, but that the defendant company, the mortgagee, had reasonable cause to believe both these things. It had such reasonable cause if it had that, the reasonable effect of having which was such a belief. To have such a thing was to know such a thing. The requirement, therefore, is that the mortgagee knew that, the reasonable effect of knowing which, was such belief. It seems to point

tain sense, because of this difference in the meaning of the term 'insolvency' they do apply so far as they determine the principles of law by which it is to be ascertained whether a creditor receiving a preference had reasonable cause to believe that the debtor had not at the time, property sufficient, at a fair valuation, to pay all of his debts."

Coder v. Arts, 18 A. B. R. 513, 152 Fed. 943 (C. C. A. Iowa): "If such a mortgage or lien creates a preference under § 60a, it is nevertheless not voidable under section 60b unless the creditor who receives it or is benefited thereby, had reasonable cause to be-

lieve that it was intended to give a preference by it."

Coder v. Arts, 22 A. B. R. 1, 213 U. S. 223: "Manifestly this conveyance could not be set aside under the provisions of section 60b. For, while it is true that, under the facts found, the conveyance might be deemed a preference, as a transfer of property which would have the effect of enabling one creditor to obtain a larger percentage of his debt or claim than other creditors of the same class, yet as it is distinctly found that neither the mortgagee nor his agent had any reasonable cause to believe that it was intended to give a preference, the same could not be avoided under § 60b."

to acknowledge of something short of insolvency, and that the mortgage covered such greater percentage. And it would seem that, to comply therewith, it is not necessary that it appear just what the mortgagee knew. If he acted as if he so believed, the reasonable inference therefrom should be that he had the required knowledge, even though it may not appear just what that knowledge was. The burden was on the plaintiff to establish each one of these three essentials."

[Since Amendment of 1910] *Ridgeway v. Kendrick*, 31 A. B. R. 497, 208 Fed. 849 (C. C. A. N. J.): "We agree that no grounds exist for setting aside the mortgage to Headley. It cannot be avoided as a preference because the evidence shows clearly that Headley did not have reasonable cause to believe that a preference was intended." [Manifestly the court meant, instead of the words "preference was intended" to say, "preference would be effected thereby" since the case arose subsequent to the amendment of 1910 to § 60b.]

In explicating this ninth element requisite to make the preference voidable, the following propositions will be useful:

§ 1396. **Existence of Reasonable Cause, Question of Fact.**—The question of the existence of the reasonable cause for so believing is a question of fact.²²

22. *Ridge Ave. Bk. v. Sundheim* (Bank v. Sundheim), 16 A. B. R. 863 (C. C. A. Penn., affirming *Sundheim v. Bk.*, 15 A. B. R. 132). See *Hackney v. Raymond Bros. Clarke Co.*, 10 A. B. R. 213 (Supt. Ct. Neb.) (this case was reversed, on other grounds, in 13 A. B. R. 164), 68 Neb. 624; *Turner v. Fisher*, 13 A. B. R. 243 (D. C. Calif.); *Upson v. Mt. Morris Bk.*, 14 A. B. R. 6 (N. Y. Sup. Ct. App.); *Deland v. Miller*, 11 A. B. R. 744, 119 Iowa 368; *Wetstein v. Franciscus*, 13 A. B. R. 326, 133 Fed. 900 (C. C. A. N. Y.); *Crittenden v. Barton*, 5 A. B. R. 775 (N. Y. Sup. Ct. App. Div.). *Obiter*, *Johnson v. Anderson* (Neb.), 11 A. B. R. 303. Note to *In re Jacobs*, 1 A. B. R. 518 (D. C. La.).

Decisions Negating Existence of "Reasonable Cause" under Act of 1867, Additionally Strong under Act of 1898.—Decisions under the Act of 1867, wherein the court has found "reasonable cause" not to have existed, are additionally strong under the present act because insolvency, formerly, consisted in the inability to meet claims as they matured, while by the present act a much broader test is prescribed. On the other hand, those which find reasonable cause existed are now weaker as precedents against the preferred creditor. *Getts v. Janesville Wholesale Grocery Co.*, 21 A. B. R. 9, 163 Fed. 417 (D. C. Wis.).

Instances before Amendment of 1910 where the facts have been held sufficient to indicate a "reasonable

cause for believing:" Mortgagee, although loaning on present consideration, yet knowing of insolvency of debtor and of debtor's intent to prefer relatives with proceeds, and actually assisting in preferring with the proceeds: *In re Bartheleme*, 11 A. B. R. 67 (Ref. N. Y.).

Assignment of insurance policy: *In re Graham*, 6 A. B. R. 750 (D. C. Ills.).

Creditor reading in newspaper of suits being started, thereupon inquiring at debtor's office, dunning the debtor frequently and finally getting chattel mortgage: *Crittenden v. Barton*, 5 A. B. R. 775 (N. Y. Sup. Ct. App. Div.).

Debtor, already owing the creditor, borrows more from him in order to cover a defalcation, loses his position and his principal endorser dies, such facts being known to the creditor: held to constitute reasonable grounds for belief: *Sebring v. Wellington*, 6 A. B. R. 671 (N. Y. Sup. Ct. App. Div.).

Brother of bankrupt agreeing not to record mortgage: and afterwards, insisting on full payment: *Rogers v. Page*, 15 A. B. R. 502, 140 Fed. 596 (C. C. A. Tenn.).

Creditor being obliged to dun the debtor repeatedly and finally taking as security the assignment of certain judgments owned by the bankrupt: *English v. Ross*, 15 A. B. R. 373, 140 Fed. 630 (D. C. Penn.).

Information that the debtor was hard up and knowledge of circumstances indicative of same state. Fail-

Kaufman v. Treadway, 12 A. B. R. 684, 195 U. S. 271: "Whether the bankrupt was insolvent on August 4, 1898, when he paid the money to his brother, the defendant, and whether the latter had reasonable cause to believe that it was intended thereby to give a preference, are questions of fact determined by the verdict of the jury and not open to review in this court."

Sundheim v. Ridge Ave. Bk., 15 A. B. R. 132, 138 Fed. 951 (D. C. Pa., affirmed sub nom. *Ridge Ave. Bk. v. Sundheim*, 16 A. B. R. 863): "And whether or not

ure to investigate will not excuse where the information was sufficient to have put the ordinary man on inquiry: *Crandall v. Coats*, 13 A. B. R. 712, 113 Fed. 965 (D. C. Iowa).

Knowledge of debtor's failure to pay debts: payment by return of goods, not cash in the ordinary course of business: consulting a lawyer and inquiring about solvency and finding close margin: In *re Andrews*, 14 A. B. R. 247, 135 Fed. 599 (D. C. Mass.).

Knowledge that debtor's business was bad and that he was being pressed, he eventually selling out business four days before bankruptcy and making payment from the proceeds: *Thomas v. Adelman*, 14 A. B. R. 510, 136 Fed. 973 (D. C. N. Y.).

Creditor knowing debtor had nothing, was behind in her payments and owed claim and that some business houses had discontinued selling to her, took assignment of insurance policy after fire: In *re Graham*, 6 A. B. R. 750 (D. C. Ills.).

Creditors inducing insolvent debtors to transfer entire stock in trade to creditor's clerk: then commingling same with their own and misleading other creditors to believe same was purchased from third party and was only small in amount: held sufficient to warrant setting aside the bill of sale as a preference: In *re Frank v. Musliner*, 9 A. B. R. 229, 76 App. Div. (N. Y.) 617. Why would these facts not warrant a finding also that the conveyance was made to hinder and delay creditors?

Knowledge of protest of debtor's notes—necessity of placing claims in hands of attorney for collection—knowledge of financial embarrassment. In *re Thomas Deuschle & Co.* (No. 2), 25 A. B. R. 348, 182 Fed. 435 (D. C. Pa.).

"Well, go ahead and fix it up and I will take my chances" of bankruptcy. *Alexander v. Redmond*, 24 A. B. R. 620, 180 Fed. 92 (C. C. A. N. Y.).

Each partner deeding his residence to importunate creditor of firm, although firm claims to have several thousand dollars outstanding on building contracts, uncollectible. *Brewster*

v. Goff, 21 A. B. R. 239, 164 Fed. 127 (D. C. Pa.).

Persistent failure to meet obligations, careful abstinence of creditor from making enquiries when getting the transfer, etc. *Huttig Mfg. Co. v. Edwards*, 20 A. B. R. 349, 160 Fed. 619 (C. C. A. Iowa).

Short of funds, unable to raise money, drafts being protested at bank, tells creditor so at time of transfer, makes general assignment same day as transfer. *Clingman v. Miller*, 20 A. B. R. 360, 160 Fed. 326 (C. C. A. Kans.).

Receiving pay on eve of bankruptcy, after repeated dunning; always receiving, as response to calls, "Mr. — is out;" pledging of equity of redemption in stock already pledged, knowledge of rumors of debtor's precarious financial condition. *Wright v. Skinner Mfg. Co.*, 20 A. B. R. 527, 162 Fed. 315 (C. C. A. N. Y.).

Mortgage to bank, withheld from record by agreement, filed within 5 days of bankruptcy, along with other facts. In *re Hickerson*, 20 A. B. R. 682, 162 Fed. 345 (D. C. Idaho).

Bank receiving \$3,000 from attorneys of bankrupt after he had absconded and after a void involuntary bankruptcy petition had been filed against him, having loaned to him originally on pledges of accounts of a customer which were repudiated by the customer as not owing because the goods were not ordered. *Pratt v. Columbia Bank*, 18 A. B. R. 406, 157 Fed. 137 (D. C. N. Y.).

President of bankrupt corporation, who had signed note as surety causing corporation to pay note to relieve himself from liability. *Kobusch v. Hand*, 19 A. B. R. 379, 156 Fed. 660 (C. C. A. Mo.).

Settlement of creditor's bill within four months, where statement of debtor's financial condition drawn from the books by an expert accountant was inspected by creditor's attorney during negotiations. In *re Mayo Contracting Co.*, 19 A. B. R. 551, 157 Fed. 469 (D. C. Mass.).

Creditor, a corporation, intrusting large sums to bankrupt, its treasurer, to invest, facts showing existence of

the facts and circumstances in the possession of the defendant in this case, at the time the payments were made to it, were sufficient to cause an ordinarily prudent business man to conclude a preference was intended, was a question for the jury and not for the court."

Rutland County Nat'l Bk. v. Graves, 19 A. B. R. 446, 156 Fed. 168 (D. C. Vt.): "We are to look at these parties at the time this payment was made, as viewing

reasonable cause, *Dulany v. Waggonman*, 22 A. B. R. 36 (D. C. Sup. Ct.).

Western Tie & Timber Co. v. Brown, 12 A. B. R. 111, 129 Fed. 728 (C. C. A. Ark., reversed in 13 A. B. R. 447, 196 U. S. 502); *In re Tindal*, 18 A. B. R. 773, 155 Fed. 456 (D. C. S. C.); *Stevens v. Oscar Holway Co.*, 19 A. B. R. 399, 156 Fed. 90 (D. C. Me.); *Nat'l Bank v. Abbott*, 21 A. B. R. 436, 165 Fed. 852 (C. C. A. Mo.); *Hackney v. Raymond Bros. Clarke Co.*, 10 A. B. R. 213 (reversed in 13 A. B. R. 164, 68 Neb. 624); *In re Teague*, 2 A. B. R. 168 (D. C. Ind.).

Instances since Amendment of 1910 where the facts have been held sufficient to indicate existence of "reasonable cause for belief:"

Asking further loan whilst preceding loan, on which bankrupt had begun business, many months overdue, creditor receiving mortgage at time of making last loan. *In re Herman*, 31 A. B. R. 243, 207 Fed. 594 (D. C. Iowa).

Accommodation endorser inducing bankrupt to discharge obligation in order to relieve him from liability. *Lazarus v. Eagan*, 30 A. B. R. 287, 206 Fed. 518 (D. C. Pa.).

Where a debtor of a bank who had agreed to maintain at all times a deposit amounting to at least 25 per cent of notes purchased had failed for a long time to keep the agreement, and the bank knew that the debtor was without cash and that numerous creditors were pressing him and threatening to throw him into bankruptcy, held sufficient notice of facts to constitute reasonable grounds for belief. *Tilt v. Citizens Trust Co.*, 27 A. B. R. 320, 191 Fed. 441 (D. C. N. J.), affirmed in *Citizens Trust Co. v. Tilt*, 29 A. B. R. 906, 200 Fed. 410 (C. C. A. N. J.).

Where the debtor was knowingly and hopelessly insolvent and the bank knew that all his real estate was covered by mortgages to nearly its full value, that his personal property was incumbered, that he was offering his business for sale and making overdrafts, held the bank was put on inquiry and was chargeable with reasonable cause to believe that bankrupt was insolvent and that a preference would be effected. *In re Thomas*, 29

A. B. R. 945, 199 Fed. 214 (D. C. N. Y.).

After several years without even collecting interest, creditor begins suddenly to urge giving of security. *Mayes v. Palmer*, 31 A. B. R. 225, 208 Fed. 971 (C. C. A. Mo.).

Where debtor had obtained a loan from a bank on his note which was renewed from time to time, and a short time after the note finally became due executed a mortgage to the bank at which time it was generally known that the bankrupt was in great financial difficulties, held reasonable cause for believing. *In re Hirshowitz*, 28 A. B. R. 571, 199 Fed. 202 (D. C. Pa.).

Instances where facts held insufficient to establish "reasonable cause for belief:"

Chattel mortgage six-sevenths for a present loan and one-seventh to pay a past debt: mortgagee not chargeable with having had reasonable ground for believing a preference was intended by the mere fact that it knew the six-sevenths were to be used in paying up debts (they being eventually in fact so used) where the debts it had knowledge of were small in comparison with what it understood to be the value of the assets: *Stedman v. Bk. of Monroe*, 9 A. B. R. 4, 117 Fed. 237 (C. C. A. Iowa).

Creditor acted in good faith after personal examination of debtor's books, from which books the debtor had concealed a large indebtedness but for which indebtedness he would have been solvent at the time of the transfer: *Brown v. Guichard*, 7 A. B. R. 515 (Sup. Ct. N. Y.).

Fair business transaction without suspicion of fraudulent preference: *In re Eggert*, 3 A. B. R. 541, 98 Fed. 843 (D. C. Wis., affirmed in 4 A. B. R. 449, 102 Fed. 735).

Creditors of employee working on salary and also on percentage of profits knowing firm insolvent but relying on law of his State that such employee was not a partner can not be said to have had reasonable grounds of belief that a preference was intended although such employee eventually was held to be a partner: *Jacobs v. Van Sickel*, 10 A. B. R. 519, 123 Fed. 340

the situation with ordinary common sense. What did they understand the condition and financial standing of the payee to be?"

And circumstances which might be inconclusive if separately considered, may, by their joint operation, be sufficient.

In re McDonald & Sons, 24 A. B. R. 446, 178 Fed. 487 (D. C. S. Car.): "Positive proof of collusion between debtor and creditor, by which one may be preferred, is not generally to be expected, and for that reason, among others, the

(D. C. N. J., affirmed in 11 A. B. R. 470, 127 Fed. 62).

Information of creditor in taking chattel mortgage that chattels about to be sold for \$2000.00 more than debts: *Hussey v. Dry Goods Co.*, 17 A. B. R. 512, 148 Fed. 598 (C. C. A. Kans.).

Bankrupts, commission merchants doing all their business through another firm of commission merchants, proceeds of sale within the four months period not recoverable preferences in absence of proof of reasonable grounds for believing preference was intended: *Ryttenberg v. Schefer*, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.).

Wife held not to have had reasonable cause of belief: In re Block, 15 A. B. R. 750, 142 Fed. 674 (C. C. A. N. Y.).

Other cases: *Hastings v. Fithian*, 13 A. B. R. 676 (N. J. Ct. Errors & App.); *Off v. Hakes*, 15 A. B. R. 699, 142 Fed. 364 (C. C. A. Ills.); *Western Tie & Timber Co. v. Brown*, 13 A. B. R. 447, 196 U. S. 502, reversing 12 A. B. R. 111; *Tomlinson v. Bk. of Lexington*, 16 A. B. R. 632 (C. C. A. N. Car.); In re Pfaffinger, 18 A. B. R. 807, 154 Fed. 528 (D. C. Ky.).

Where bankrupt was largely indebted to the creditor corporation, and the president of the latter purchased all of the bankrupt's stock, and during the 11 months he was connected with both concerns the indebtedness was not reduced, nor any effort made to reduce it, upon the resignation of the president of the creditor corporation, creditor ceased its sales to bankrupt and demanded payment of its account, held insufficient to show reasonable cause for belief. *Benner v. Blummauer-Frank Drug Co.*, 28 A. B. R. 798, 198 Fed. 362 (D. C. Wash.).

Instance where facts held insufficient to establish "reasonable cause to believe." General manager of bankrupt's branch store, ignorant of conditions of other branches and of bankrupt's condition generally. In re Greenberger, 30 A. B. R. 117, 203 Fed. 583 (D. C. N. Y.).

Bank, knowing that debtor had shipped part of his stock to Honolulu and securing an attachment because of the

shipment, but ignorant of the existence of other creditors, the debtor having no defense but consenting to immediate trial which was followed by judgment, held insufficient to show that the bank had reasonable cause to believe preference over other creditors would be obtained. *Stanley v. Pajaro Valley Bank*, 28 A. B. R. 467, 196 Fed. 365 (C. C. A. Cal.).

Bank, learning debtor owes other banks contrary to his financial statement takes judgment, and threatens levy, but received pay along with explanation that omission of debts to other banks was because they were personally secured by collateral and were "going to reorganize" because of internal dissensions. *Hamilton Bank v. Balcomb*, 24 A. B. R. 338, 177 Fed. 155 (C. C. A. Ills.).

Demand note of corporation, discounted for ninety days, paid before due at request of bank, whose president had loaned \$30,000 and taken as security \$30,000 worth of goods belonging to the bankrupt's store and had placed them for sale in the store of a corporation of which he was principal stockholder, the debtor being insolvent in fact but not known to be so, but on the contrary having a high rating, the reason for the transaction given by the debtor corporation being that its principal stockholder had been sued in large amount for alienation of wife's affections. *Powell v. Gate City Bank*, 24 A. B. R. 316, 178 Fed. 610 (C. C. A. Mo.).

Creditors who received payments from the proceeds of a sale, and who believed that all creditors were paid a pro rata amount, will not be obliged to surrender such payments prior to proving their claims, even though they knew that the debtor was financially embarrassed. In re Varley, etc., Co., 26 A. B. R. 840, 188 Fed. 761 (D. C. Ala.).

Taking debtor as surety on note, notwithstanding suspicious circumstances. *Getts v. Janesville Wholesale Grocery Co.*, 21 A. B. R. 5, 163 Fed. 417 (D. C. Wis.).

Bankrupt had a fire; got insurance

law allows a resort to circumstances as the means of ascertaining the truth, and the rule of evidence is well settled that circumstances inconclusive if separately considered may by their joint operation, especially when corroborated by moral coincidences, be sufficient. Signs of insolvency were too many and too marked not to warn the president of this bank that he was getting a prohibited advantage over other creditors. The facts are so persuasive that they would have given reasonable ground for suspicion to persons far less astute and less accustomed to the ways of business in general than was the president of this bank." Quoted further at § 1410.

The question is one for the jury,²³ where the action is one at law, yet where the facts are established, then as matter of law the court may direct a verdict as in other cases;²⁴ but not so where the facts are not established sufficiently to have authorized a directing of a verdict in other cases.²⁵

The adjudication of bankruptcy does not establish the existence of reasonable cause for belief on the creditor's part.²⁶

§ 1397. Preferential Transfer Not Necessarily Fraudulent.—The action is not one for fraud. A preference is not necessarily fraudulent.²⁷

money; creditor, a bank, knowing such facts, procured payment of notes out of insurance money, desiring to secure pay before complications arose. *Irish v. Citizens Trust Co.*, 21 A. B. R. 39 (D. C. N. Y.).

Lumber company needing funds, borrows, but real cause of failure seizure of timber by United States government. *McDonald v. Clearwater R. Co.*, 21 A. B. R. 182, 164 Fed. 1007 (U. S. C. C. Idaho).

Unrequested repayment of loan with letter stating money can no longer be used. *Wright v. Sampter*, 18 A. B. R. 355, 152 Fed. 196 (D. C. N. Y.).

Debtor reputed to be wealthy farmer had made financial statements year before showing net worth \$100,000, transfer not inclusive of all property. *Coder v. Arts*, 18 A. B. R. 513, 152 Fed. 943 (C. C. A. Iowa).

Merely reasonable cause of belief that debtor insolvent, not enough. In re First Nat'l Bk. of Louisville, 18 A. B. R. 766, 155 Fed. 100 (C. C. A. Ky.).

Fire insurance policies transferred, circumstances insufficient. In re Neill-Pinckney-Maxwell Co., 22 A. B. R. 401, 170 Fed. 481 (D. C. Pa.).

Creditor relinquishing personal endorsement of stockholder in exchange for mortgage on bankrupt corporation's assets, but without knowledge of the insolvent condition of the debtor. In re Evans Lumber Co., 23 A. B. R. 881, 176 Fed. 643 (D. C. Ga.).

Cotton merchants receiving security from local cotton broker who becomes bankrupt. In re Peacock, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.).

Other instances, miscellaneous. In re Tindal, 18 A. B. R. 773, 155 Fed. 456 (D. C. S. Car.); *Stevens v. Oscar Holway Co.*, 19 A. B. R. 399, 156 Fed. 90 (D. C. Me.); *Utah Ass'n of Credit Men v. Boyle Fur. Co.*, 26 A. B. R. 867 (Sup. Ct. Utah); In re Frazin & Oppenheim, 29 A. B. R. 214, 201 Fed. 86 (C. C. A. N. Y.); In re Richards, Inc., 28 A. B. R. 636 (Ref. Dist. Col., affirmed by Sup. Ct. Dist. Col.); *Powell v. Gate City Bank*, 24 A. B. R. 317, 178 Fed. 610 (C. C. A. Mo.); *Stern v. Paper Co.*, 25 A. B. R. 451, 183 Fed. 228 (D. C. N. D.).

23. *Kaufman v. Treadway*, 12 A. B. R. 684, 195 U. S. 271; *Christopherson v. Oleson*, 102 N. W. 685 (Sup. Ct. S. Dak.).

24. *Christopherson v. Oleson*, 102 N. W. 685 (Sup. S. Ct. Dak.).

25. *Upson v. Mt. Morris Bk.*, 14 A. B. R. 6 (N. Y. Sup. Ct. App. Div.).

26. Compare post, § 1777; also see *Laundy v. Nat'l Bk.*, 11 A. B. R. 223 (Sup. Ct. Kans.); *Hussey v. Dry Goods Co.*, 17 A. B. R. 513, 148 Fed. 598 (C. C. A. Kans.).

27. See ante, §§ 113, 1305. *Little v. Hardware Co.*, 13 A. B. R. 429, 133 Fed. 874 (C. C. A. Tex.); *Baden v. Bertenshaw*, 11 A. B. R. 308 (Sup. Ct. Kans.); *Upson v. Mt. Morris Bk.*, 14 A. B. R. 6 (N. Y. Sup. Ct. App.); In re Duffy, 9 A. B. R. 360, 118 Fed. 926 (D. C. Penn.); *Githens v. Shiffler*, 7 A. B. R. 453, 112 Fed. 505 (D. C. Penn.); In re Belknap, 12 A. B. R. 329, 129 Fed. 646 (D. C. Penn.); *Fry v. Pennsylvania Trust Co.*, 5 A. B. R. 53 (opinion of Com. Pleas); *Chism v.*

Coder v. Arts, 22 A. B. R. 1, 213 U. S. 223: "A consideration of the provisions of the bankruptcy law as to preferences and conveyances shows that there is a wide difference between the two, notwithstanding they are sometimes spoken of in such a way as to confuse the one with the other. A preference, if it have the effect prescribed in § 60, enabling one creditor to obtain a greater portion of the estate than others of the same class, is not necessarily fraudulent. Preferences are set aside when made within four months, with a view to obtaining an equal distribution of the estate, and in such cases it is only essential to show a transfer by an insolvent debtor to one who, himself or by his agent, knew of the intention to create a preference. In construing the Bankruptcy Act this distinction must be kept constantly in mind. As was said in *Githens v. Shiffler*, 112 Fed. 505: 'An attempt to prefer is not to be confounded with an attempt to defraud, nor a preferential transfer with a fraudulent one.' In *re Maher*, 144 Fed. 503-505, it was well said by the district court of Massachusetts: 'In a preferential transfer the fraud is constructive or technical, consisting in the infraction of that rule of equal distribution among all creditors which it is the policy of the law to enforce when all cannot be fully paid. In a fraudulent transfer the fraud is actual—the bankrupt has secured an advantage for himself out of what in law should belong to his creditors, and not to him.'"

Crooks v. People's Nat. Bk., 3 A. B. R. 238, 46 App. Div. N. Y. 335: "Under this statute the question of fraud does not enter; it is the result or effect of the act done that is declared against, not the manner nor method by which it is done, no matter how circuitous the method may be. If the effect of a transfer of property made within four months * * * is to enable any of the bankrupt's creditors to obtain a greater percentage of his debt than others of the same class, then such transfer is voidable if the person receiving it or to be benefited thereby had reasonable cause to believe that it was intended thereby to give a preference."

But it is not a joinder of inconsistent causes of action to allege the transaction alternatively, as whether a preference or a fraudulent conveyance.²⁸

§ 1398. Creditor Need Not Actually Know, nor Actually Believe.

—It is not necessary to prove the creditor himself actually knew of the debtor's intent or condition;²⁹ nor is it necessary to prove the creditor him-

Bk., 5 A. B. R. 56, 77 Miss. 599; In *re Block*, 15 A. B. R. 752, 142 Fed. 674 (C. C. A. N. Y.); *Manning v. Evans*, 19 A. B. R. 217, 156 Fed. 106 (D. C. N. J.); In *re Kullberg*, 23 A. B. R. 758, 176 Fed. 585 (D. C. Minn.); *Eichholz v. Polack*, 25 A. B. R. 243 (App. Div. N. Y.); *Templeton v. Wollens*, 29 A. B. R. 208, 200 Fed. 257 (C. C. A. N. Y.).

28. Compare post, § 1739. *Wright v. Skinner*, 14 A. B. R. 500, 136 Fed. 694 (D. C. N. Y.); *Bryan v. Madden*, 11 A. B. R. 763, 78 N. Y. Supp. 220; *Pratt v. Christie*, 12 A. B. R. 1, 95 App. Div. 282; inferentially, *Laundy v. Bk.*, 11 A. B. R. 223 (Sup. Ct. Kans.).

29. In *re Jacobs*, 1 A. B. R. 518 (D. C. La.), and note. *Hackney v. Raymond Bros. Clarke Co.*, 10 A. B. R. 213 (reversed on the facts in 13 A. B. R. 164), 68 Neb. 624; *Crittenden v.*

Barton, 5 A. B. R. 777 (Sup. Ct. App. N. Y.); In *re Eggert*, 4 A. B. R. 452, 107 Fed. 735 (C. C. A. Wis.); note to *Crooks v. People's Nat'l Bk.*, 3 A. B. R. 238 (N. Y. Sup. Ct. App. Div.); *Sundheim v. Ridge Ave. Bk.*, 15 A. B. R. 132, 138 Fed. 951 (D. C. Penn., affirmed sub. nom. *Ridge Ave. Bk. v. Sundheim*, 16 A. B. R. 863); *English v. Ross*, 15 A. B. R. 374, 140 Fed. 630 (D. C. Penn.); compare, *Western Tie & Timber Co. v. Brown*, 13 A. B. R. 451, 196 U. S. 502; In *re Hines*, 16 A. B. R. 497, 144 Fed. 543 (D. C. Penn.); In *re Mills Co.*, 20 A. B. R. 501, 162 Fed. 42 (D. C. N. Car.); *Rogers v. Fidelity Sav. Bank & Loan Co.*, 23 A. B. R. 1, 172 Fed. 735 (D. C. Ark.); *Brewster v. Goff Lumber Co.*, 21 A. B. R. 106, 164 Fed. 124 (D. C. Pa.), quoted at § 1410; (1867) *Burfee v. First Nat'l Bk.*, 9 N.

self actually believed.³⁰

Rogers, Trustee v. Am. Halibut Co., 31 A. B. R. 576 (Mass.): "It is unnecessary to show actual knowledge or belief by the creditor."

In *re Andrews*, 14 A. B. R. 247, 135 Fed. 599 (D. C. Mass.): "Hardy, whatever his actual belief, had reasonable cause to believe that Andrews was insolvent."

Pratt v. Columbia Bank, 18 A. B. R. 406, 157 Fed. 137 (D. C. N. Y.): "The meaning of the words 'reasonable cause to believe' has been too often the subject of decision to require extended citation of authority. Knowledge is not necessary, nor even belief, but only reasonable cause to believe, which is a very different thing."

And it is no defense for the creditor to prove that actually he did not so believe.³¹

Thus, the mere fact that the creditor was a young lady, unacquainted with business affairs, who did not appreciate the significance of the facts, was held to be no excuse; the real test being what deduction or inference the ordinary business man would have drawn from the same facts.

Obiter, Wright v. Sampter, 18 A. B. R. 355, 152 Fed. 196 (D. C. N. Y.): "The peculiarity of this case is that the mind to be affected is that of a confiding niece, wholly unacquainted with business knowledge, and however intelligent and prudent in matters within her own experience, incapable of comprehending the significance of business facts, which would have been more than enlightening to men of the business world. It is therefore urged by the defendants that *Barbour v. Priest*, 103 U. S. 293, justifies the proposition that not only must the facts exist and be sufficiently impressive to make inquiry in such minds as are catalogued in the cases above cited, but they must be sufficient to impress their significance upon the mind of the person to be affected—in this case a woman leading a life apart from the world of business. It was indeed said in the case last cited (one inducing great sympathy for the preferred creditor) that it is 'necessary to prove the existence of this reasonable cause of

B. Reg. 314; In *re McDonald & Sons*, 24 A. B. R. 446, 178 Fed. 487 (D. C. S. Car.), quoted at § 1410; *obiter, Dougherty v. First Nat. Bank*, 28 A. B. R. 263, 197 Fed. 241 (C. C. A. Ohio); *Shale v. Farmers' Bank*, 25 A. B. R. 888 (Kans.), quoted at § 1399; *Hewitt v. Boston Strawboard Co.*, 31 A. B. R. 652 (Mass.).

30. In *re Jacobs*, 1 A. B. R. 518 (D. C. La.); *Hackney v. Raymond Bros. Clarke Co.*, 10 A. B. R. 213, reversed on the facts in 13 A. B. R. 164, 68 Neb. 624; *Crittenden v. Barton*, 5 A. B. R. 777 (N. Y. Sup. Ct.); In *re Eggert*, 4 A. B. R. 452, 107 Fed. 735 (C. C. A. Wis.); note to *Crooks v. People's Nat'l Bk.*, 3 A. B. R. 238 (N. Y. Sup. Ct. App. Div.); *Sundheim v. Ridge Ave. Bk.*, 15 A. B. R. 132, 138 Fed. 951 (D. C. Penn.); In *re Vir-*

ginia Hardwood Mfg. Co., 15 A. B. R. 135, 139 Fed. 209 (D. C. Ark.); In *re Hines*, 16 A. B. R. 497, 144 Fed. 543 (D. C. Penn.); *English v. Ross*, 15 A. B. R. 374, 140 Fed. 630 (D. C. Pa.); *Rogers v. Fidelity Sav. Bk. & Loan Co.*, 23 A. B. R. 1, 172 Fed. 735 (D. C. Ark.); *Hewitt v. Boston Strawboard Co.*, 31 A. B. R. 652 (Mass.); *Shale v. Farmers Bank*, 25 A. B. R. 888 (Kans.), quoted at § 1399; In *re McDonald & Sons*, 24 A. B. R. 446, 178 Fed. 487 (D. C. S. Car.), quoted at § 1410.

31. In *re Hines*, 16 A. B. R. 497, 144 Fed. 543 (D. C. Penn.); *Shale v. Farmers Bank*, 25 A. B. R. 888 (Kans.), quoted at § 1399. Compare, to such general effect, *Hamilton Bank v. Balcomb*, 24 A. B. R. 338, 177 Fed. 155 (C. C. A. Ill.).

belief * * * in the mind of the preferred party' (p. 296). But these words must be taken in conjunction with the whole opinion, which was written in express consonance with *Grant v. Bank*, supra, and the phrase quoted. I take to assume in 'the preferred party' the mind of 'an ordinarily intelligent man.' It would be intolerable that the voidability of a preference should depend not upon the effect of facts admittedly or by proof known to a defendant, but upon the degree of intelligence or experience which such defendant was capable of exercising in respect thereto; such a rule would put a premium upon ignorance and encourage the assumption thereof. The rule here applicable is therefore; would an ordinarily intelligent and prudent business man have had reasonable cause to believe upon any facts known to Miss Sampter that her uncle intended to prefer herself, her sister and mother? I think not." This case is further quoted at § 1399.

§ 1399. Sufficient if Circumstances Such as to Raise Inference of Belief on Creditor's Part.—It is sufficient to prove that the circumstances, all taken together, were such as would naturally have led an ordinary business man to believe.³²

Rogers v. American Halibut Company, 31 A. B. R. 576 (Mass.): "If the circumstances are such as would lead the ordinary prudent man of affairs to the conclusion that his debtor is insolvent, he obtains a preferential payment within the meaning of the statute by accepting payment in whole or in part of the debt, where the transaction takes place within four months prior to adjudication and other creditors of the same class, because of the greater percentage received, must accept decreased dividends. *Hewitt v. Boston Strawboard Co.*, 214 Mass. 260; *Wilson v. Mitchell-Woodbury Co.*, 214 Mass. 514."

32. *Buchanan v. Smith*, 16 Wall. 277; *Dutcher v. Wright*, 94 U. S. 553; *Bank v. Cook*, 95 U. S. 343; In re *Virginia Hardwood Mfg. Co.*, 15 A. B. R. 135, 139 Fed. 209 (D. C. Ark.); *Benedict v. Deshell*, 11 A. B. R. 20, 68 N. E. 999; In re *Jacobs*, 1 A. B. R. 518 (D. C. La.); *Crooks v. People's Nat'l Bk.*, 3 A. B. R. 238, 46 App. Div. N. Y. 335; *Hackney v. Raymond Bros. Clarke Co.*, 10 A. B. R. 213, reversed in 13 A. B. R. 164, 68 Neb. 624; In re *Andrews*, 14 A. B. R. 247, 135 Fed. 599 (D. C. Mass.): Payment by return of goods and not by cash in the usual course of trade, coupled with knowledge that debtor does not pay debts. *Crittenden v. Barton*, 5 A. B. R. 775 (N. Y. Sup. Ct. App. Div.); *Upson v. Mt. Morris Bk.*, 14 A. B. R. 6 (N. Y. Sup. Ct. App. Div.); In re *Beerman*, 7 A. B. R. 431, 112 Fed. 663 (D. C. Ga.); *Parker v. Black*, 16 A. B. R. 205, 143 Fed. 560 (D. C. N. Y., affirmed in 18 A. B. R. 15); In re *Hines*, 16 A. B. R. 497, 144 Fed. 543 (D. C. Penn.); In re *Hickerson*, 20 A. B. R. 682, 162 Fed. 345 (D. C. Idaho); In re *Mills Co.*, 20 A. B. R. 501, 162 Fed. 42 (D. C. N. Car.); *Wright v. Skinner Mfg. Co.*, 20 A. B. R. 527, 162 Fed. 315 (C.

C. A. N. Y.); *Brewster v. Goff Lumber Co.*, 21 A. B. R. 106, 164 Fed. 124 (D. C. Pa.), quoted at § 1410; *Whitwell, trustee, v. Wright*, 23 A. B. R. 747 (N. Y. Sup. Ct. App. Div.); *Huntington v. Baskeville*, 27 A. B. R. 219, 192 Fed. 813 (C. C. A. S. D.); In re *McDonald & Sons*, 24 A. B. R. 446; 178 Fed. 487 (D. C. S. Car.), quoted at § 1410; *Stern v. Paper*, 25 A. B. R. 451, 183 Fed. 228 (D. C. N. D.); In re *Richards*, 28 A. B. R. 636, (Sup. Ct. Dist. Columbia); In re *Gibson*, 27 A. B. R. 401, 191 Fed. 665 (D. C. S. D.); In re *Dorr*, 28 A. B. R. 505, 196 Fed. 292 (C. C. A. Cal.), quoted at § 1410; In re *The Leader*, 26 A. B. R. 668, 190 Fed. 624 (D. C. Ark.); In re *Martin*, 27 A. B. R. 151 (D. C. Tex.); *Spencer v. Nekemoto*, 24 A. B. R. 517 (D. C. Hawaii); instance, In re *Harrison Bros.*, 28 A. B. R. 684, 197 Fed. 320 (D. C. Pa.); *McGirr v. Humphreys Grocery Co.*, 26 A. B. R. 518 (D. C. Ohio).

And the assertions of the creditor as to his actual lack of belief are not to be controlling. *Hamilton Bank v. Balcomb*, 24 A. B. R. 338, 177 Fed. 155 (C. C. A. Ills.).

Hewitt v. Boston Strawboard Co., 31 A. B. R. 652 (Mass.): "Where there is reasonable cause to believe that at the date of the transfer within the statutory period, the debtor is insolvent and payment is accepted of a debt overdue, it is immaterial whether the creditor actually believes what may have been disclosed as to the true state of affairs."

Alexander v. Redmond [before Amendment of 1910], 24 A. B. R. 620, 180 Fed. 92 (C. C. A. N. Y.): "If he has reasonable cause to believe that that person is insolvent and has also reasonable cause to believe that the effect of the transfer will be to enable the transferee to obtain a greater percentage of his debt than any other creditor of the same class, the requirements of the concluding part of § 60 are fully met."

Bardes v. First National Bank of Hawarden, 12 A. B. R. 771, 122 Iowa 443: "We concede the legal proposition contended for in behalf of defendants that a mere suspicion of financial embarrassment is not enough to charge the creditor with knowledge of insolvency. * * * But it is enough to constitute a reasonable cause to believe him insolvent that the facts and circumstances with reference to the debtor's financial condition which are brought home to the creditor are such as would put an ordinarily prudent man upon inquiry, which, if pursued, would lead to knowledge of insolvency."

In *re Eggert*, 4 A. B. R. 449, 102 Fed. 735 (C. C. A. Wis., affirming 3 A. B. R. 341): "It is not essential that the creditor should have actual knowledge of, or belief in, his debtor's insolvency, but that he should have reasonable cause to believe his debtor to be insolvent; that if facts and circumstances with respect to the debtor's financial condition are brought home to him, such as would put an ordinarily prudent man upon inquiry, the creditor is chargeable with knowledge of the facts which such inquiry should reasonably be expected to disclose."

Toof v. Martin, 13 Wall. 40: "It is a general principle that every one must be presumed to intend the necessary consequences of his acts. The transfer, in any case, by a debtor, of a large portion of his property, while he is insolvent, to one creditor, without making provision for an equal distribution of its proceeds to all of his creditors, necessarily operates as a preference to him, and must be taken as conclusive evidence that a preference was intended, unless the debtor can show that he was at the time ignorant of his insolvency, and that his affairs were such that he could reasonably expect to pay all his debts. * * * The burden of proof is upon him in such case, and not upon the assignee or contestant in bankruptcy. * * * The Statute, to defeat the conveyances, does not require that the creditors should have had absolute knowledge on the point, nor even that they should, in fact, have had any belief on the subject. It only requires that they should have had reasonable cause to believe that such was the fact. And reasonable cause they must be considered to have had when such a state of facts was brought to their notice in respect to the affairs and pecuniary condition of the bankrupts as would have led prudent business men to the conclusion that they could not meet their obligations as they matured in the ordinary course of business ['insolvency' under Act of 1867]."

Sundheim v. Ridge Ave. Bk., 15 A. B. R. 132, 134, 138 Fed. 951 (D. C. Pa., affirmed sub nom. *Bank v. Sundheim*, 16 A. B. R. 863): "Reasonable cause to believe that it was intended to give a preference does not require proof that the defendant had either actual knowledge or actual belief, but only such surrounding circumstances as would lead an ordinarily prudent business man to conclude that a preference was intended."

Ogden v. Reddish, 29 A. B. R. 531, 200 Fed. 977 (D. C. Ky.): "One may suspect, believe, or know that such a thing is so, without any interest or desire to

have it otherwise; but he cannot fear that it is so without such interest or desire. These mental states are separate and distinct from each other. They do not shade off into one another. Possibly, where a creditor suspects his debtor is insolvent, he also fears that he is. At any rate, he readily passes from the one state to the other. Now, the only one of these four mental states which the statute calls for is knowledge. It does not use the word 'know,' but that which is its equivalent, to wit, 'shall have reasonable cause to believe.' Having reasonable cause to believe is knowing that the reasonable effect of knowing which is belief, or that which reasonably should cause belief. There are different degrees of knowledge which it is possible for the preferred creditor to have. He may know that the debtor is insolvent, and that the transfer to him covers a greater percentage of his property than he is entitled to, and hence that it effects a preference. Possibly this is a greater degree of knowledge than called for by the terms of the statute, but it is within its intent. For if a lesser degree of knowledge suffices, certainly the greater degree is not to be excluded. Then comes, not such knowledge, but knowledge of that the reasonable effect of knowing which is belief to that effect. This degree of knowledge is called for in so many words. Then comes knowledge of that the reasonable effect of knowing which is not such belief, but only a fear or suspicion that such is the case. Such a degree of knowledge is certainly not within the words of the statute.

"The problem I have been considering is whether it is ever possible for a case where the preferred creditor has only such a degree of knowledge to come within the statute, and, if so, on what basis does it come within it? The conviction reached has been that it is possible. If the degree of knowledge is such as to engender fear that such is the case, so strong that the preferred creditor refrains from availing himself of the means at his hand for ascertaining the truth, in order to keep himself in the dark in regard thereto, and to be in position to claim that he did not have reasonable cause to believe that the transfer to him would work a preference, the case is covered by the statute. It is brought within the statute by holding that he had constructive knowledge of what he would have ascertained, had he inquired, and the effect of constructive knowledge is the same always as actual."

The test is, What inference would the ordinarily intelligent business man draw from the facts?

Wright v. Sampter, 18 A. B. R. 355, 152 Fed. 196 (D. C. N. Y.): "The rule is equally well established that it is sufficient if the facts brought home to the person sought to be affected are such as would produce action and inquiry on the part of 'an ordinarily intelligent man' (*Grant v. Bank*, 97 U. S. 80); 'a prudent business man' (*Bank v. Cook*, 95 U. S. 343; *Toof v. Martin*, 13 Wall. 40); 'a person of ordinary prudence and discretion' (*Wager v. Hall*, 16 Wall. 584); 'an ordinarily prudent man' (*In re Eggert*, 4 Am. B. R. 449); 'a prudent man' (*Dutcher v. Wright*, 94 U. S. 553)." This case further quoted at § 1398.

Coder v. McPherson, 18 A. B. R. 523, 152 Fed. 951 (C. C. A. Iowa): "Notice of facts which would incite a man of ordinary prudence to an enquiry under similar circumstances is notice of all the facts which a reasonably diligent inquiry would disclose."

Compare, *In re Pfaffinger*, 18 A. B. R. 807, 154 Fed. 528 (D. C. Ky.): "The test is whether the creditor who is charged with having received a voidable preference had at the time of receiving it such information as ought to have led a reasonably prudent man to the conclusion that a preference was thereby intended, and this includes, as we have seen, the necessary element

of sufficient information of the affairs of the debtor as ought to lead a reasonably prudent man to the conclusion that he was then insolvent. Mere suspicion of insolvency is not sufficient, nor is mere unwillingness to trust further. Some authorities, indeed, fix a test to the effect that the creditor must be regarded as having been preferred if at the time of the transfer or payment he had information sufficient to put a reasonably prudent man upon inquiry, which if made and pursued would lead to a full knowledge of the debtor's condition. Such a rule must have a reasonable construction, and to make it operate justly, must relate to information of the financial condition and property of the debtor, and not merely to whether he had already borrowed from the creditor quite as much or more money than the latter thought it was best to lend to him for other and different reasons."

Thus, the resort to unusual methods of payment or securing of payment will raise an inference of belief that a preference was within the contemplation of the parties.³³

Shale v. Farmers Bank, 25 A. B. R. 888 (Kans.): "Conceding that the bank has the right to set off a depositors account against a matured indebtedness due the bank, it appears that in this case the payment was not made by the bank applying the depositors account to the payment, but by a check which it had required the bankrupt to give in payment of notes not due. A payment under somewhat similar circumstances was held to constitute a preference in *Ridge Ave. Bank v. Sundheim*, 16 A. B. R. 863, 145 Fed. 798 (C. C. A. 3d Cir.). To the same effect is *Irish v. Citizens Trust Co.*, 21 A. B. R. 39, 163 Fed. 880 (D. C. N. Y.), where it was held that a bank cannot charge a debtor's account or receive a check in payment of note it holds, which is not yet due, without constituting a preference under the bankruptcy law. The mere statement of the cashier that he did not believe that Summerfelt was in failing circumstances did not require that the case should be submitted to the jury, in view of the undisputed facts. Proof of actual knowledge or actual belief on the part of the officers of the bank was not required. To constitute a preference it is only necessary to show that the creditor had reasonable cause to believe that a preference was intended ["would be obtained" since amendment of 1910]."

Similarly, the taking of a mortgage or other transfer of substantially all

33. *In re Andrews*, 14 A. B. R. 247, 135 Fed. 599 (D. C. Mass.): Return of goods not cash.

But see *Laundy v. First Nat'l Bk.*, 11 A. B. R. 223 (Sup. Ct. Kans.), where it was held, that the depositing of book accounts as security with the creditor was not sufficient. Yet this was a most extraordinary proceeding it would seem. Business men do not usually resort to the pledging of their book accounts until they are in extremis.

Wright v. Skinner Mfg. Co., 20 A. B. R. 527, 162 Fed. 315 (C. C. A. N. Y.), which was a case of pledging equity of redemption in stock already pledged; *In re Bailey & Son*, 21 A. B. R. 911, 166 Fed. 982 (D. C. Pa.), where goods were set apart and marked to secure an accommodation

endorser; *Coleman v. Decatur Egg Case Co.*, 26 A. B. R. 249, 186 Fed. 136 (C. C. A. Mo.), quoted in this same section (§ 1399); *In re McDonald & Sons*, 24 A. B. R. 446, 178 Fed. 487 (D. C. S. Car.), quoted at §§ 1406, 1410; *Tilt v. Citizens Trust Co.*, 27 A. B. R. 320, 191 Fed. 441 (D. C. N. J.), affirmed *Citizens Trust Co. v. Tilt*, 29 A. B. R. 906, 200 Fed. 410 (C. C. A. N. J.).

But compare *Newman v. Dry Goods Co.*, 31 A. B. R. 399 (Kansas City Court of Appeals), wherein a jury returned a verdict under evidence that would seem clearly to have proved the existence of reasonable cause for belief, though appellate court could not rule that it was sufficient as matter of law to warrant a reversal.

of a debtor's property, knowing it to be such, and that other creditors existed, will constitute a preference "with reasonable cause of belief."³⁴

McElvain v. Hardesty, 22 A. B. R. 320, 169 Fed. 31 (C. C. A. Mo.): "Moreover, if McElvain did not have actual knowledge of the insolvent condition of his debtors, we think in the circumstances of this case he is constructively chargeable with that knowledge. He took a transfer of all his debtor's property—of a going concern—in satisfaction of a debt. This, in itself, was an unusual thing, and the reasons which actuated it must have sprung from a fear or suspicion of danger."

In re *Virginia Hardwood Mfg. Co.*, 15 A. B. R. 142, 139 Fed. 209 (D. C. Ark.): "He knew that his mortgage covered so much of the assets that what was left was totally insufficient to pay the other creditors listed on the statement. If he really believed that the bankrupt had (as the statement shows) assets amounting to \$104,288.80, and that he was taking practically all of it, and excluding creditors (as the statement shows) who held claims aggregating \$13,518.78, he knew that he was getting security far in excess of his claim, and that the effect of it was to hinder and delay the other creditors. * * *

"The same rule is true where a single creditor, with a knowledge of the insolvency of its debtor, takes a mortgage upon substantially all of its assets with the knowledge at the time (as will appear later) that there were outstanding creditors of nearly \$49,000, which was the situation in the case at bar when this mortgage was taken."

Pollock v. Jones, 10 A. B. R. 616, 124 Fed. 163 (C. C. A. S. Car.): "It is true that it is said that no good reason existed for supposing that Mr. Pollock knew of this insolvency. It is to be remarked, however, that in getting security Pollock obtained and accepted a mortgage of the entire assets of the firm. * * *

"Yet, by taking this mortgage, covering and controlling their entire stock of goods of every description in their possession, present and future, he practically made the firm at that instant insolvent to the extent, at least, of appropriating all the assets of the firm to the payment of one favored creditor, and if these be required to pay him in full, leaving nothing for other creditors."

And the request and agreement to withhold a mortgage from the records indicates such reasonable cause.³⁵

Likewise, the sale of an entire stock of merchandise is a suspicious circumstance.³⁶

Much more is the acceptance of payment out of the stock of trade where no investigation of values was had, nor any inquiry into the debtor's financial condition and almost the entire stock in trade was thus transferred.

Coleman v. Decatur Egg Case Co., 26 A. B. R. 249, 186 Fed. 136 (C. C. A. Mo.): "The proof shows that on this occasion Vail made no inquiries touching the debts or the assets of the debtor. The whole transaction consumed but a few moments. He saw the stock and necessarily knew what he proposed to take would deprive his debtor of the great bulk of its stock in trade and would cripple it for continued business. He said on his examination that he did not

34. In re *McDonald & Sons*, 24 A. B. R. 446, 178 Fed. 487 (D. C. S. Car.), quoted at § 1406; *Eichholz v. Polack*, 25 A. B. R. 243 (App. Div. N. Y.).

35. *Rogers v. Page*, 15 A. B. R. 505, 140 Fed. 596 (C. C. A. Tenn.).

36. Compare, §§ 1216, 1494.

know anything that would lead him to believe that his debtor was then insolvent, but he admits that he had suspicions.

" * * *. It was an unusual transaction for a creditor to require payment of his merchandise debts out of stock in trade of the debtor and especially so, to go to the extent of taking nearly all of it. The record also seems to disclose a purpose to avoid securing information touching the financial condition of the debtor. Sources of true information concerning it were available to the defendant at the time its president took the stock. The books were there. The debtor who was familiar with his business was there. But neither the books were asked for nor was any question put to the debtor concerning its assets or liabilities. The creditor knew or must have known that by taking practically all his stock in trade he was taking away from his debtor, the means of prosecuting his business."

It has apparently been held even that proof of current rumor and gossip is admissible.³⁷

§ 1400. Cause for Belief Simply That Preference Would Result—Debtor's Intent Immaterial.—By the Amendment of 1910 the cause for belief on the creditor's part is no longer that a preference was "intended" to be given by the bankrupt, but, rather, that a preference would be effected.³⁸

Herron Co. v. Moore, 31 A. B. R. 221, 208 Fed. 134 (C. C. A. Cal.): "Under the Bankruptcy Act, § 60, as amended by the act of 1910, it is no longer necessary, in order to establish a preference, to prove the existence of the debtor's intent to prefer. It is sufficient if it is shown that the creditor

37. Inferentially, *Spencer v. Neke-moto*, 24 A. B. R. 517 (D. C. Hawaii).

38. Bankr. Act, as amended 1910, § 60 (b): "If a bankrupt shall have procured or suffered a judgment to be entered against him in favor of any person or have made a transfer of any of his property, and if, at the time of the transfer, or of the entry of the judgment, or of the recording or registering of the transfer if by law recording or registering thereof is required, and being within four months before the filing of the petition in bankruptcy or after the filing thereof and before the adjudication, the bankrupt be insolvent and the judgment or transfer then operate as a preference, and the person receiving it or to be benefited thereby, or his agent acting therein, shall then have reasonable cause to believe that the enforcement of such judgment or transfer would effect a preference, it shall be voidable by the trustee and he may recover the property or its value from such person." In re *Starkweather & Albert*, 30 A. B. R. 743, 206 Fed. 797 (D. C. Mo.); instance, In re *Shantz & Son Co.*, 30 A. B. R. 552, 205 Fed. 425 (D. C. N. Y.), quoted at § 1300; *Merklein v.*

Hurley, 28 A. B. R. 841, 197 Fed. 183 (D. C. N. Y.).

The change effected by the Amendment of 1910 does not however affect the judicial interpretation of the phrase "Reasonable cause to believe." *Pratt v. Columbia Bank*, 18 A. B. R. 406, 157 Fed. 137 (D. C. N. Y.).

Decisions Ignoring Amendment.—A good many decisions have been rendered in cases arising since the Amendment of 1910 wherein the courts, apparently unmindful of the Amendment, have continued to speak of the necessity of proving the reasonable cause for belief to be reasonable cause for belief that a preference "was intended" rather than would be "effected." Instance, *Newman v. Dry Goods Co.*, 31 A. B. R. 399 (Kansas City Court of Appeals), quoted at § 1277 note; *Mayes v. Palmer*, 31 A. B. R. 225, 208 Fed. 97 (C. C. A. Mo.); In re *Greenberger*, 30 A. B. R. 117, 203 Fed. 583 (D. C. N. Y.); *Grant v. National Bank of Auburn*, 28 A. B. R. 712, 197 Fed. 581 (D. C. N. Y.); In re *Varley, etc., Co.*, 26 A. B. R. 840, 188 Fed. 761 (D. C. Ala.); *Aiello v. Crampton*, 29 A. B. R. 1, 201 Fed. 891 (C. C. A. N. Mex.).

receiving the alleged preference payment had, at the time when it was made, reasonable cause to believe that the bankrupt was insolvent, and that in accepting and retaining the same he would receive a larger per cent of his debt than the other creditors of the same class. It is not disputed that, on the date when the payment were made to the appellant, the bankrupt was hopelessly insolvent. It is not disputed that the result of the payments was to give the appellant a greater percentage of its claim than other creditors of the same class. But it is earnestly contended that the evidence falls short of showing that, at the time of the payment of the money or the transfer of the property by the bankrupt to the appellant, the latter had reasonable cause to believe that the payment or the transfers would effect the preference prohibited by the Bankruptcy Act."

In *re Harrison*, 28 A. B. R. 684, 197 Fed. 320 (D. C. Pa.): "This amendment obviates the necessity of proving (1) the existence of the debtor's intent to prefer, (2) the cause for belief on the part of the creditor that a preference was intended, and (3) that the debtor knew his insolvency. The test now is, whether the person receiving the payment, or to be benefited thereby, or his agent acting therein, at the time the payment was made, had reasonable cause to believe that the bankrupt was then insolvent and that in accepting and retaining said payment, he would receive a larger percentage of his debt than any other creditor of the same class."

In *re Herman*, 31 A. B. R. 243, 207 Fed. 594 (D. C. Iowa): "Under the section as so amended, if the bankrupt be in fact insolvent, it is only necessary that the person receiving the transfer, or his or her agent acting therein, shall have reasonable cause to believe that the enforcement of such transfer will effect a preference, to render the transfer voidable by the trustee."

Logically, it is the creditor's knowledge or belief that a preference would be effected that should be the test rather than his knowledge or belief of the debtor's intention to prefer.

Report No. 691 of Senate Judiciary Committee of the 61st Congress, Second Session.

"Further, the Amendment of 1903, making the existence of 'reasonable cause to believe' on the creditor's part a prerequisite to the trustee's right to recover the preference from him, required that this reasonable cause of belief should be that a 'preference was intended to be given,' rather than that a 'preference would be effected.' Logically, it is the creditor's knowledge or belief that a preference would be effected that should be the test, rather than his knowledge or belief of the debtor's intention to prefer."

It is the knowledge of the effect on the creditor's assets that constitutes the wrong doing.

§ 1401. Belief That Preference Would Be Effected May Be Presumed.—Belief on the creditor's part that a preference would be effected by the transaction may be presumed.

Hewitt v. Boston Strawboard Co., 31 A. B. R. 652 (Mass.): "The bankrupt and the defendant must be presumed to have known that what had been done resulted in a preference, even if the form of the transfer consisted of securities received by the bankrupt from a third party."

Before the Amendment of 1910 rendered it unnecessary to prove belief in the debtor's intent, it was nevertheless held that the belief of the existence

of such intent might be presumed, and that where a creditor had reasonable grounds to believe the debtor insolvent, and where the obvious effect of the receipt of the money or other property in satisfaction of the obligation under these circumstances was to give him an advantage over other creditors, he was chargeable with notice of intention to prefer.³⁹

English v. Ross, 15 A. B. R. 374, 140 Fed. 630 (D. C. Pa.): " * * * and, now that it has turned against him, he cannot be heard to say that he did not know he was getting a preference or that one was contemplated. Where that is the necessary result of a transaction it is conclusively presumed to have been intended."

Obiter, [*Western*] *Tie & Timber Co. v. Brown*, 13 A. B. R. 451, 196 U. S. 502: "This conclusion, moreover, is the result of the finding that Harrison had no intention to give the tie company a preference, for if Harrison, being insolvent, to the knowledge of the company, within the prohibited period, gave to the tie company authority to collect the sums due to him by the laborers for goods sold them, with the right, or even the option to apply the money to prior debt due by Harrison to the company, the necessary result of the transaction would have been to create a voidable preference. And if the inevitable result of the transaction would have been to create such a preference, then the law would conclusively impute to Harrison the intention to bring about the result necessarily arising from the nature of the act which he did. *Wilson v. City Bank*, 17 Wall. 486, 21 L. Ed. 727. To give effect, therefore, to the finding that there was no intention on the part of Harrison to prefer, we must consider that the authority given by him to the tie company to collect from the laborers did not give that company the right, or endow it with the option, when it had collected, to retain the money for its exclusive benefit, and to the detriment of the other creditors of Harrison.

"The result of the facts found, then, is this: Harrison sold his goods to the laborers, and agreed with the tie company that that company, when it paid the laborers, should deduct the amount due by the laborers from the wages which the tie company owed them, and, after making the deduction, should remit to Harrison the amount thus deducted, irrespective of any indebtedness otherwise due by Harrison to the tie company. Did this give rise to a voidable preference within the intendment of § 57g and § 60b of the Bankrupt Act?

"In view of the necessary result of the findings which we have previously pointed out, it is, we think, beyond doubt that the agreement was not voidable preference within the meaning of the statute, since, considering the agreement alone, it brought about no preference whatever."

Coder v. McPherson, 18 A. B. R. 523, 152 Fed. 951 (C. C. A. Iowa): "In the face of this knowledge, it took these mortgages which, in the aggregate,

³⁹. *Hackney v. Hargreaves Bros.*, 13 A. B. R. 169, 68 Neb. 624; impliedly, *In re Andrews*, 14 A. B. R. 247, 135 Fed. 599 (D. C. Mass.).

Compare, similar holdings as to presumptions of debtor's intent to prefer as an act of bankruptcy, ante, § 132. Compare, under State preference law, *Wright v. Gansevoort*, 17 A. B. R. 326 (N. Y. Sup. Ct.).

Impliedly, *Clingman v. Miller*, 20 A. B. R. 360, 160 Fed. 326 (C. C. A. Kans.); *Burgoyne v. McKillip*, 25 A.

B. R. 387, 182 Fed. 452 (C. C. A. Neb.); *Kimmerle v. Farr*, 26 A. B. R. 818, 189 Fed. 295 (C. C. A. Mich.); *In re Door* [Before Amendment of 1910 to § 60 (b) therefore "intended" instead of "effected"] 28 A. B. R. 505 (C. C. A. Calif.); *Wickwir v. Webster, etc.*, Bank, 27 A. B. R. 157 (Sup. Ct. Ia.); *In re Martin*, 27 A. B. R. 151 (D. C. Tex.); inferentially (but not directly), *In re McDonald & Sons*, 24 A. B. R. 446, 178 Fed. 487 (D. C. S. Car.), quoted at § 1410.

covered substantially all the unexempt property the debtor owned except a few hogs and horses. The real estate was already mortgaged according to Armstrong's second statement for \$147,500, and it took mortgages upon this land and a chattel mortgage upon his tools, machinery, and crops. The inevitable effect of these incumbrances was to deprive the unsecured creditors of every means of collecting their debts; for these mortgages withdrew from attachment and execution substantially all the debtor's unexempt property. The legal presumption is that parties intend the inevitable effect of their acts, and, in view of all these facts, the conclusion is irresistibly borne in upon our minds that * * * the bank * * * when it took these mortgages, had reasonable cause to believe that it was intended thereby to give it a preference over other creditors of the same class."

In *re Hines*, 16 A. B. R. 499, 144 Fed. 142 (D. C. Pa.): "In thus monopolizing the last available asset that the debtor had to deal with, he could but know that he was getting more than his share if Hines proved insolvent, to which everything pointed. Of this he took the risk, and now that it has gone against him he cannot be heard to say that he did not know he was getting a preference, or that one was contemplated. When that is the necessary result of a transaction, it is conclusively presumed to have been intended."

And the creditor's denial of any knowledge that he was getting a preference will be unavailing.⁴⁰

English v. Ross, 15 A. B. R. 374, 140 Fed. 630 (D. C. Pa.): "Monopolizing, as he thus did, all the available assets of the bankrupt, the defendant could not but know that he was getting more than his share, if Mangan proved insolvent, to which everything pointed, and of which he was therefore affected with notice."

§ 1402. Reasonable Cause for Belief of Insolvency Requisite.—

Reasonable cause for belief that a preference would be effected by the transaction necessarily involves reasonable cause to believe that the debtor was in fact insolvent.⁴¹ And this means reasonable cause for belief that his assets at fair valuation do not equal his liabilities.⁴²

In *re Andrews*, 16 A. B. R. 390 (C. C. A. Mass.): "This [the new definition of insolvency in the Act of 1898] has established so artificial a rule that the

40. In *re Hines*, 16 A. B. R. 497, 144 Fed. 142 (D. C. Penn.); *Sundheim v. Ridge Ave. Bank*, 15 A. B. R. 134 (affirmed sub nom. *Bank v. Sundheim*, 16 A. B. R. 863, D. C. Penn.); instance, In *re Thomas Deutschle & Co.* (No. 2), 25 A. B. R. 348, 182 Fed. 430 (D. C. Pa.).

Obiter, court holding proof of existence of reasonable cause of belief insufficient, *Hamilton Bank v. Balcomb*, 24 A. B. R. 338, 177 Fed. 155 (C. C. A. Ills.).

41. *Merklein v. Hurley*, 28 A. B. R. 841, 197 Fed. 183 (D. C. N. Y.); In *re Lorch & Co.*, 28 A. B. R. 784, 199 Fed. 944 (D. C. Ky.); In *re Carlile*, 29 A. B. R. 373, 199 Fed. 612 (D. C. N. Caro.); *Shelton v. First Nat. Bank*, 27 A. B. R. 587 (Sup. Ct. Okla.).

Before Amendment of 1910; There-

fore "Intended" Instead of "Effected." —*Savings Bk. v. Jewelry Co.*, 12 A. B. R. 781, 123 Iowa 432; In *re Eggert*, 4 A. B. R. 457, 102 Fed. 735 (C. C. A. Wis.); In *re Hines*, 16 A. B. R. 497, 144 Fed. 142 (D. C. Penn.); *Hussey v. Dry Goods Co.*, 17 A. B. R. 514, 148 Fed. 598 (C. C. A. Kans.); In *re Goodhile*, 12 A. B. R. 374, 130 Fed. 471 (D. C. Iowa); *Johnson v. Anderson*, 11 A. B. R. 294 (Neb.); *Baden v. Bertenshaw*, 11 A. B. R. 308, 68 Kans. 32; *Brewster v. Goff Lumber Co.*, 21 A. B. R. 106, 164 Fed. 124 (D. C. Pa.); In *re Pfaffinger*, 18 A. B. R. 807, 154 Fed. 528 (D. C. Ky.), quoted at § 1399; In *re Kullberg*, 23 A. B. R. 758, 176 Fed. 585 (D. C. Minn.).

42. In *re Pettingill & Co.*, 14 A. B. R. 758, 135 Fed. 218 (C. C. A. Mass.); *Suffel v. Nat'l Bk.*, 16 A. B. R. 262, 106 N. W. 837 (Wis.).

usual indicia by virtue of which a man is regarded as insolvent, and, consequently, by virtue of which a creditor may be said to have reason to believe that he is insolvent, or the reverse, become, to a very large extent, of no importance."

Thus, a transfer to secure not only a pre-existing debt, but also to secure repayment of money advanced at the time to a debtor with which to make a composition with his other creditors, has been upheld, since, though the facts were sufficient to put the transferee upon inquiry and such transferee knew that he was getting his claim secured in full whilst other creditors were getting but a percentage, yet, the facts were not sufficient, after investigation, to show that the assets were really worth less than the amount of the debts.

In *re Bartlett*, 22 A. B. R. 891, 172 Fed. 679 (D. C. Pa.): "The bankrupt, of course, was embarrassed, his condition being such that he had to go to his trade creditors with a compromise. But embarrassment is not always insolvency, although it suggests it, and the bank was, therefore, put on inquiry. The bank knew also that it was being secured in full, where other creditors were getting but a fraction. And while it supposed that all the indebtedness outside of its own, except that of Frederick Job, was taken care of by the compromise, it ran the chance of there being others, and, as it now turns out, the bankrupt also owed his wife and uncle. There are other considerations, however, by which the bank is blameless. It may be conceded that, except for the compromise, the bankrupt was insolvent, his indebtedness being close to \$12,000, and his assets, at top figures, several hundred dollars less than that. But if he was, the bank had no idea of it. And they took pains to inform themselves. * * * The bankrupt, also, three months before that, had made a statement, showing that he was worth a good deal more than this, which to a certain extent, they had the right to rely on. And the very offer of a compromise suggested an excess of assets, without which there was no inducement for it.

And, either actual knowledge of the debtor's insolvent condition or at any rate actual knowledge of such facts as would have put the creditor on inquiry seems to be necessary.

In *re Houghton Web Co.*, 26 A. B. R. 202, 185 Fed. 213 (D. C. Mass.): "* * * it is clear that the creditor cannot be said to have had reasonable cause to believe such a preference was intended, unless the evidence shows that it knew, or ought to have known, the substantial truth as to the bankrupt's financial condition. Actual knowledge of the facts on its part is not charged by the trustee. He contends that there are circumstances shown which put the bank upon inquiry and render it chargeable with the knowledge which would have been obtained by due inquiry."

§ 1403. Also of All Other Elements of Preference.—Merely to establish grounds which reasonably would have caused the creditor to believe the debtor insolvent is not enough.⁴³

⁴³ In *re First Nat'l Bk. of Louisville*, 18 A. B. R. 766, 155 Fed. 100 (C. C. A. Ky.), quoted at §§ 1400, 1405. Obiter, contra, *McMurtrey v. Smith*, 15 A. B. R. 435 (Master's Report

adopted by D. J.). Compare, also, *Johnson v. Anderson*, 11 A. B. R. 294 (Neb.).

Merely Reasonable Ground of Belief of "Insolvency" Apparently Con-

Cullinane v. State Bank, 12 A. B. R. 776, 123 Iowa 340: "The bank must have reasonable cause to believe not only that insolvency existed as a fact, but that a preference was intended."

Babbitt v. Kelly, 9 A. B. R. 338 (Mo. Ct. App.): "To invalidate a preference, the party benefited, or his agent, must have reasonable cause to believe, not that the debtor is insolvent, but that a preference is intended, the act says: that this involves knowledge by the preferred creditor or his agent, or reasonable cause to believe, that the debtor is insolvent at the time of the alleged preferential act, for the essence of a preference denounced by the Bankrupt Law is that it is given by an insolvent debtor."

Contra, *In re Andrews*, 14 A. B. R. 247, 135 Fed. 599 (D. C. Mass.): "If the debtor is insolvent, he intends preference by any payment of a pre-existing debt. If the creditor has reasonable cause to believe that the debtor is insolvent then the creditor has reasonable cause to believe that a preference is intended."

The proof must also show reasonable grounds for believing that the other seven elements of a preference existed, namely, that the debtor had made a "transfer" of his property, or suffered a judgment to be taken, etc., that the effect thereof would be to give one creditor a greater percentage of his debt than some other of the same class, etc., etc.⁴⁴

sidered Sufficient.—Many of the reported decisions seem to imply, that the reasonable ground of belief to be proved is merely as to the debtor's insolvency. *In re Virginia Hardwood Mfg. Co.*, 15 A. B. R. 135, 139 Fed. 209 (D. C. Ark.); *Johnson v. Anderson*, 11 A. B. R. 294 (Neb.).

In re Andrews, 14 A. B. R. 247, 135 Fed. 599 (D. C. Mass., reversed, on this point, in 16 A. B. R. 391): "If the debtor is insolvent he intends preference by any payment of a pre-existing debt. If the creditor has reasonable cause to believe that the debtor is insolvent, then the creditor has reasonable cause to believe a preference is intended.

Suffel v. Nat'l Bk., 16 A. B. R. 259, 106 N. W. (Wis.) 837; *In re Beerman*, 7 A. B. R. 431, 112 Fed. 663 (D. C. Ga.); *In re King*, 7 A. B. R. 619, 113 Fed. 110 (D. C. Mass.).

And one case even holds that the petition must allege that the creditor had reasonable grounds for belief not only that a preference was intended but also that the debtor was insolvent. *Hicks v. Langhorst*, 6 A. B. R. 178 (Com. Pleas Ohio), and note.

This is incorrect: **reasonable grounds for belief that a preference was intended, includes reasonable ground for belief that the debtor was insolvent.** *Savings Bank v. Jewelry Co.*, 12 A. B. R. 781, 123 Iowa 432.

In re Eggert, 3 A. B. R. 541, 98 Fed. 843 (affirmed in 4 A. B. R. 449, 102

Fed. 735, D. C. Wis.): "To constitute a voidable preference, as defined in §§ 60a, 60b, the creditor must have reasonable cause to believe the debtor to be insolvent in fact, as the foundation for reasonable cause to believe that an unlawful preference is intended;" hence the latter allegation is superfluous, although as evidence it is admissible.

Some few cover the entire field, however. See *Johnson v. Anderson*, 11 A. B. R. 294 (Sup. Ct. Neb.); compare, *Baden v. Bertenshaw*, 11 A. B. R. 308, 68 Kans. 32.

Compare, also, *In re Goodhile*, 12 A. B. R. 374, 130 Fed. 471 (D. C. Iowa): "Under the present law, this decision of the Supreme Court (*Merchants' Bank v. Cook*, 95 U. S. 342) would require that the condition of the debtor's affairs must be known to be such that prudent business men would conclude that the aggregate of the debtor's property at a fair valuation, was not sufficient to pay his debts' before there is reasonable cause to believe the debtor is insolvent and that a preference would therefore be the result of a payment while in such condition."

44. *Hackney v. Raymond Bros. Clarke Co.*, 10 A. B. R. 213, 68 Neb. 624 (reversed in 13 A. B. R. 164); inferentially, *Bank v. Sundheim*, 16 A. B. R. 865 (C. C. A. Penn.); *Cullinane v. State Bank*, 12 A. B. R. 779, 123 Iowa 340; *Turner v. Fisher*, 13 A. B.

Thus, the preferred creditor must be proved to have had reasonable cause to believe a greater per cent would be obtained thereby by him than other creditors would receive.⁴⁵

For instance, where a debtor pays some creditors under a settlement made with all, but has not enough to pay the others, it must be proved that the creditors who were paid had reasonable ground for believing the debtor would be unable to pay all alike.⁴⁶

§ 1404. **Burden of Proof.**—The burden of proof of the existence of the reasonable cause of belief is on the trustee,⁴⁷ as well as of each element of the preference.⁴⁸ But where the transfer complained of was made to a relative, that fact is important in determining whether the burden has been sustained.⁴⁹

§ 1405. **Mere Cause to Suspect Debtor's Insolvency Not Enough.**—Merely because some cause to suspect insolvency of the debtor exists is not enough: there must be such a knowledge of facts as would induce a reasonable belief in the ordinary man that a preference would result [formerly, that the debtor "intended" to give a preference.]⁵⁰

R. 243, 133 Fed. 594 (D. C. Calif.); *Reber v. Shulman & Bro.*, 24 A. B. R. 782, 179 Fed. 574 (D. C. Pa.).

45. [Before Amendment of 1910; therefore "intended" instead of "effected."] In *re Armstrong*, 16 A. B. R. 593 (D. C. Iowa).

Instance, bank knowing that debtor had shipped part of his stock to Honolulu and securing an attachment because of the shipment, but ignorant of the existence of other creditors, the debtor having no defense but consenting to immediate trial which was followed by judgment, held insufficient to show bank had reasonable cause to believe preference over other creditors would be obtained. *Stanley v. Pajaro Valley Bank*, 28 A. B. R. 467, 196 Fed. 365 (C. C. A. Cal.).

46. *Smith v. Hewlett Robin Co.*, 24 A. B. R. 153, 178 Fed. 271 (C. C. A. N. Y.).

47. *Calhoun Co. Bank v. Cain*, 18 A. B. R. 509, 152 Fed. 983 (C. C. A. W. Va.); *Getts v. Janesville Grocery Co.*, 21 A. B. R. 5, 163 Fed. 417 (D. C. Wis.).

48. *Reber v. Shulman & Bro.*, 24 A. B. R. 782, 179 Fed. 574 (D. C. Pa.); *Keith v. Gettysburg Nat'l Bk.*, 10 A. B. R. 762 (23 Penn. Sup. Ct. 14); compare, *In re Chappell*, 7 A. B. R. 608, 113 Fed. 545 (D. C. Va.), although this was a case of "innocent" preferences; *In re Pfaffinger*, 18 A. B. R. 807, 154 Fed. 528 (D. C. Ky.); (*Butler Paper Co. v. Goebel*, 16 A. B. R. 26,

143 Fed. 296 (C. C. A. Ills.). See ante, § 775½; post, § 1768.

49. Compare, even stronger statement of the rule, *In re Sanger*, 22 A. B. R. 145, 169 Fed. 722 (D. C. W. Va.), wherein the court even holds that in such cases the burden shifts.

50. *Bardes v. Bank*, 12 A. B. R. 771, 122 Iowa 443; *Stevenson v. Milliken Tomlinson*, 13 A. B. R. 201, 99 Me. 320 (Sup. Jud. Ct. Me.); *Turner v. Fisher*, 13 A. B. R. 243, 133 Fed. 594 (D. C. Calif.); *Off v. Hakes*, 15 A. B. R. 699, 142 Fed. 364 (C. C. A. Ills.); *Upson v. Mt. Morris Bk.*, 14 A. B. R. 6 (N. Y. Sup. Ct. App.); *Keith v. Gettysburg Nat'l Bk.*, 10 A. B. R. 762, 23 Penn. Sup. Ct. 14; *In re Eggert*, 4 A. B. R. 449, 102 Fed. 741 (C. C. A. Wis., affirming 3 A. B. R. 541); *Hackney v. Raymond Bros. Clarke Co.*, 10 A. B. R. 213, reversed in 13 A. B. R. 164, 68 Neb. 624; *Brown v. Guichard*, 7 A. B. R. 519 (Sup. Ct. N. Y.). Also, see *Laundy v. First Nat'l Bk.*, 11 A. B. R. 223 (Sup. Ct. Kans.). But compare, *In re Beerman*, 7 A. B. R. 431, 112 Fed. 663 (D. C. Ga.); *obiter*, *Crandall v. Coats*, 13 A. B. R. 716, 113 Fed. 965 (D. C. Iowa); note to *In re Jacobs*, 1 A. B. R. 518 (D. C. La.); *Suffel v. Nat'l Bk.*, 16 A. B. R. 259, 106 N. W. (Wis.) 837; *In re Alden*, 16 A. B. R. 379 (Ref. Ohio); *inferentially*, *obiter*, *Bank v. Sundheim*, 16 A. B. R. 865 (C. C. A. Penn.); *Getts v. Janesville Grocery Co.*, 21 A. B. R. 9, 163 Fed. 417 (D. C. Wis.); *Irish v. Citizens Trust*

Grant v. National Bank, 97 U. S. 80: "It is not enough that some creditor has some cause to suspect the insolvency of his debtor, but he must have such a knowledge of facts as to induce a reasonable belief of his debtor's insolvency, in order to invalidate a security taken for his debt. To make mere suspicion a ground of nullity in such a case would render the business transactions of the community altogether too insecure. It was never the intention of the framers of the act to establish any such rule. A man may have many grounds of suspicion that his debtor is in failing circumstances and yet have no cause for a well grounded belief of the fact. He may be unwilling to trust him further; he may feel anxious about his claims, and have a strong desire to secure it; and yet such belief as the act requires may be wanting. Obtaining additional security or receiving payment of a debt under such circumstances is not prohibited by law. Receiving payment is put in the same category in the section referred to as receiving security. Hundreds of men constantly continue to make payments up to the very eve of their failure, which it would be very unjust and disastrous to set aside. And yet this could be done in a large proportion of cases if mere grounds of suspicion of their insolvency were sufficient for the purpose."

Stucky v. Masonic Savings Bank, 108 U. S. 74: "A creditor dealing with a debtor whom he may suspect to be in insolvent circumstances, but of which he may not have sufficient evidence, may receive payments without violating the bankruptcy law. He may be unwilling to trust him further: he may be anxious about his claim, and desire to secure it; but such relief as the Act requires may be wanting. Additional security and receiving payments under such circumstances are not prohibited by law."

In re Goodhile, 12 A. B. R. 374, 130 Fed. 471 (D. C. Iowa): "No doubt they were desirous of obtaining what was due them, and they may have had suspicions that she was embarrassed or might be insolvent but that is not enough."

And circumstances may seem suspicious after the bankruptcy occurs, that would not have appeared unusual at the time of their occurrence, and would then have presented no "reasonable cause" on which to found a belief of preference.⁵¹

[Before Amendment of 1910; therefore "intended to be given," rather than "would be effected."] *Powell v. Gate City Bank*, 24 A. B. R. 316, 178 Fed. 609

Co., 21 A. B. R. 39 (D. C. N. Y.); *Curtiss v. Kingman*, 20 A. B. R. 95, 159 Fed. 880 (C. C. A. Mass.); *obiter*, *Huttig Mfg. Co. v. Edwards*, 20 A. B. R. 349, 160 Fed. 619 (C. C. A. Iowa); *In re Pfaffinger*, 18 A. B. R. 807, 154 Fed. 523 (D. C. Ky.), quoted at § 1399; *impliedly*, *Stevens v. Oscar Holway Co.*, 19 A. B. R. 399, 156 Fed. 90 (D. C. Me.); *Tumlin v. Bryan*, 21 A. B. R. 319, 165 Fed. 166 (C. C. A. Ga.); *Stuart v. Farmers' Bk. of Cuba City*, 21 A. B. R. 403, 137 Wis. 66, 117 N. W. 820; *obiter*, *Nat'l Bk. v. Abbott*, 21 A. B. R. 436, 165 Fed. 852 (C. C. A. Mo.); *Sharpe v. Allender*, 22 A. B. R. 431, 170 Fed. 589 (C. C. A. Pa.); *In re Wolf Co.*, 21 A. B. R. 73, 164 Fed. 448 (D. C. Pa., affirmed sub nom. quoted at § 1409; *In re Bartlett*,

22 A. B. R. 891, 172 Fed. 679 (D. C. Pa.); *Kimmerle v. Farr*, 26 A. B. R. 818, 189 Fed. 295 (C. C. A. Mich.); *Stern v. Paper Co.*, 28 A. B. R. 592, 198 Fed. 642 (C. C. A. N. Dak.); *impliedly*, *In re Houghton Web Co.*, 26 A. B. R. 202, 185 Fed. 213 (D. C. Mass.); *Sparks v. Marsh*, 24 A. B. R. 280, 177 Fed. 739 (D. C. Ark.); *instance* (accommodation endorser where payment made not to him but to holder), *Reber v. Shulman & Bro.*, 24 A. B. R. 782, 179 Fed. 574 (D. C. Pa.); *Reber v. Louis Shulman & Bro.*, 25 A. B. R. 475, 183 Fed. 564 (C. C. A. Pa.), affirming 24 A. B. R. 782. Compare, *Carey v. Donohue*, 31 A. B. R. 210, 209 Fed. 328 (C. C. A. Ohio).

⁵¹ *Tumlin v. Bryan*, 21 A. B. R. 319, 165 Fed. 166 (C. C. A. Ga.).

(C. C. A. Mo.): "Suspicion, fear, and facts that arouse suspicion and fear in the mind of the creditor, but give no reasonable ground for him to believe that the debtor intends a preference by his payment or security, do not make such a preference voidable."

Newman v. Dry Goods Co., 31 A. B. R. 399 (Kansas City Court of Appeals): "Judicial expressions on the subject of what will and what will not constitute constructive knowledge emphasize the distinction between notice of facts and circumstances which would incite a man of ordinary prudence to an inquiry under similar circumstances and notice of circumstances that would merely excite suspicion. The former is equivalent to notice of all the facts which a reasonably diligent inquiry would disclose (*Coder v. McPherson* (C. C. A., 8th Cir. O.), 18 Am. B. R. 523, 152 Fed. 951, 82 C. C. A. 99.) while the latter is deemed insufficient to constitute reasonable cause to believe that a preference is intended, and will not put the creditor upon inquiry. * * *

"Turning to the circumstances in evidence, we find nothing in them to contradict the testimony of the credit man to the effect that, when he received the information that Curtis had sold out, he believed, and had cause to believe, that Curtis was solvent. He had before him a recent, written statement from Curtis which showed his net worth to be over \$5,000, and on the strength of that statement had just shipped a large quantity of goods to him on credit. Actions speak louder than words, and it would be impossible to think that defendant would have been willing to send goods of such value to a merchant of whose solvency it had even a doubt or suspicion, or to cause defendant to take any other step than that of sending out an agent to obtain a satisfactory settlement of its claim. It is quite an ordinary occurrence for an honest and solvent merchant to sell his business, and it is usual for creditors to regard and treat such an act as calling upon him for the immediate payment of his debts. Diligence of a creditor in such case cannot be construed as evidence of a belief or even of a suspicion that his debtor might be insolvent. The only thing that the credit man knew was that a customer he believed to be solvent had sold out, and that a satisfactory settlement of his indebtedness was in order, and should be effected with usual business celerity.

"The inference is reasonable and in fact very strong that the adjuster made the settlement in ignorance of the fact of Curtis' insolvency, and that he pursued the usual course of investigation and inquiry. He made inquiries of Curtis, the banker, the purchaser, and others, and what he heard from these various sources tended to corroborate the statement of Curtis that he had paid his other debts and had remaining available assets amounting to almost \$1000 in excess of his liabilities to defendant. Should we say, as a matter of law, that he should have made other investigations and inquiries? We think not, and hold that the question of whether or not he received notice of circumstances that would have incited a man of ordinary prudence to further inquiry is shown by all the evidence to involve an issue of fact for the jury to solve." [But the facts in this case would seem to have warranted a different verdict by the jury.]

§ 1406. Mere Giving of Unusual Security Insufficient.—Thus merely the giving of unusual security—as, for instance, the depositing with the creditor of certain book accounts as security—is not sufficient in and of itself.⁵² But agreeing to the stipulation that a mortgage is to be kept off the records is indicative of reasonable cause.

⁵². *Laundy v. First Nat'l Bk.*, 11 A. B. R. 223 (Sup. Ct. Kans.). And compare, *In re Andrews*, 16 A. B. R. 391 (C. C. A. Mass.); *McDonald v. Clearwater R. Co.*, 21 A. B. R. 182, 164 Fed. 1007 (U. S. C. C.).

Rogers v. Page, 15 A. B. R. 505, 149 Fed. 194 (C. C. A. Tenn.): "That he should agree not to record the instrument then taken until he should deem it necessary for his own protection is significant of his knowledge of his brother's condition and of the effect upon his credit if recorded. The very fact that after carrying his brother for years he should demand the immediate payment of his entire debt out of the proceeds of the sale of this land, and his exoneration from liability as surety by the payment of every debt upon which he was bound, admits of but one explanation in the light of this evidence, and that is that he knew his brother was insolvent, and that, if he was not thus preferred, he would lose a large part of his debt."

Likewise, the deeding of each partner's private residence to their importunate creditor, has been held sufficient to indicate the existence of reasonable cause, even though the firm claimed to have large outstanding accounts due them on building contracts, which they were unable to collect.⁵³ But the giving of unusual security, along with other facts, may indicate existence of the reasonable cause.⁵⁴

So, the giving of a mortgage as security for payment of a loan for which the mortgagee held the bankrupt's note will be deemed to be a preference where it appears that the bankrupt was in financial straits and that that fact was known to the mortgagee.⁵⁵

§ 1407. Mere Nonpayment of Claim Long Past Due, or Frequent Duns or Broken Promises, Not Sufficient.—Neither the mere nonpayment of the particular creditor's claim nor the fact that most of the indebtedness to the creditor is past due at the time of the payment on account and that the creditor has been urging payment and the debtor repeatedly promising it, is in itself sufficient cause for drawing the inference.⁵⁶

In *re Goodhile*, 12 A. B. R. 374, 130 Fed. 471 (D. C. Iowa): "It is true that most of the bankrupt's account with Wyman, Partridge & Co. was past due at the time of these payments, and that the company was urging payment, but that is not sufficient to charge it with reasonable cause to believe that she was insolvent. Neither is the fact that the check was dated ahead, if that were true; and, under the testimony submitted, it was not. Such facts would only show that the debtor was unable to meet payments promptly, and that is not insolvency, under the present bankruptcy law."

In *re Wolf Co.*, 21 A. B. R. 73, 164 Fed. 448 (D. C. Pa., affirmed sub nom. *Sharpe v. Allender*, 22 A. B. R. 431, 170 Fed. 589 (C. C. A.)): "The question whether the transfer was a voidable one depends on whether Mr. Allender had reasonable cause to believe that a preference was intended, that is to say, that he was getting a prohibited advantage over other creditors similarly situated. He was if the company was insolvent, but not, if it was not; and the case turns therefore on whether the signs of insolvency were such as to put him on inquiry,

^{53.} *Brewster v. Goff*, 21 A. B. R. 239, 164 Fed. 127 (D. C. Pa.).

^{54.} *Wright v. Skinner Mfg. Co.*, 20 A. B. R. 527, 162 Fed. 315 (C. C. A. N. Y.).

^{55.} In *re Hirshowitz*, 28 A. B. R. 571, 199 Fed. 202 (D. C. Pa.).

^{56.} *Brown v. Guichard*, 7 A. B. R.

519 (Sup. Ct. N. Y.). To same effect, *Turner v. Fisher*, 13 A. B. R. 243, 133 Fed. 594 (D. C. Calif.). To similar effect, *Paper Co. v. Goembel*, 16 A. B. R. 29, 143 Fed. 295 (C. C. A. Ills.). To similar effect, In *re Alden*, 16 A. B. R. 379 (Ref. Ohio).

affecting him with whatever inquiry would have discovered. It is not easy to decide, much less to point out in advance, what will amount to notice, each case standing pretty much on its own bottom. Mere financial embarrassment is not always enough, although it usually will be. The law differs somewhat in this respect from what it was formerly, owing to the different meaning given to insolvency, which, under the Act of 1867, existed if the debtor was not in a condition to pay his debts in the ordinary course of business (*Toof v. Martin*, 13 Wall. 40), but not now, unless the aggregate of his property is insufficient to meet his obligations. In the present instance, the Wolf Co. was embarrassed, and as we now know, insolvent. * * * It was plain, of course, that the Wolf Co. was in embarrassed circumstances. Its debts were known to be large, its operations extended, and some of them at least unprofitable, and new capital was needed to carry on the business. The proposed reorganization had also failed at least with the existing syndicate, and the money advanced by them had got to be repaid shortly. But, on the other hand, it did not follow from any or all of this, that the company was insolvent in the sense that its assets were not sufficient at a fair valuation to satisfy its obligations. If its debts were large, so was its plant and its business, its machinery being sold all over the United States and even as far as Japan and China. In the proposed reorganization, preferred stock to the amount of \$400,000 was to be issued, and a like amount of common, the syndicate who were to finance the operation putting up \$150,000 to take care of the outstanding bonds and getting \$180,000 of each kind of stock, W. G. Wolf on his part receiving \$170,000 of each, leaving \$50,000 of each in the treasury. If figures of this magnitude were at all justified as they apparently were in the contemplation of the parties it was hardly suggestive of insolvency. * * * The idea that Allender could go to the books is not to be thought of. Neither could he expect to get access to the report of the experts if it had been asked for. It is not intimate and inaccessible information such as this, that a creditor is bound by, but that which is open to observation and will yield to reasonable inquiry, where it has not been expressly brought home to him. No doubt in the present instance, Allender was anxious over his debt, and pressed for its payment, and may have expressed apprehension with regard to it. But this is not to be carried too far, nor made to operate too strongly against him, particularly in view of the assurances which he had received from those best calculated to know on which he had a right to rely, to the contrary."

At least such fact is not sufficient to authorize a court to find reasonable grounds for belief to be established as a matter of law,⁵⁷ but may be evidence tending to show reasonable cause for belief.⁵⁸

57. *Upson v. Mt. Morris Bk.*, 14 A. B. R. 6 (N. Y. Sup. Ct. App. Div.); *In re Eggert*, 4 A. B. R. 449, 3 A. B. R. 541, 102 Fed. 735 (C. C. A. Wis.).

58. *Inferentially*, *In re Moody*, 14 A. B. R. 276, 134 Fed. 628 (D. C. Iowa). And refusal to give further credit after receipt of security is not necessarily conclusive.

Paper Co. v. Goembel, 16 A. B. R. 29, 143 Fed. 295 (C. C. A. Ills.): "In any view the circumstance is of slight weight, as the extension of credit to purchasers is governed by various

considerations: the solvent owner of property may well be refused credit if known to be slow pay, deceitful, litigious or in litigation."

Huttig Mfg. Co. v. Edwards, 20 A. B. R. 349, 160 Fed. 619 (C. C. A. Iowa); *Wright v. Skinner Mfg. Co.*, 20 A. B. R. 527, 162 Fed. 315 (C. C. A. N. Y.); *Herron v. Moore*, 31 A. B. R. 221, 208 Fed. 134 (C. C. A. Cal.); *obiter* [reasonable cause held not to exist], *In re Houghton Web Co.*, 26 A. B. R. 202, 185 Fed. 213 (D. C. Mass.).

Inferentially, *Walburn v. Babbitt*, 16 Wall. 577: "The usual and ordinary course of Mendelson's business was to sell at retail. * * * But it is a wholly different thing when he sells his entire stock to one or more persons."

Toof v. Martin, 13 Wall. 40: "And reasonable cause they must be considered to have had when such a state of facts was brought to their notice in respect to the affairs and pecuniary condition of the bankrupts as would have led prudent business men to the conclusion that they could not meet their obligations in the ordinary course of business."

§ 1408. Receiving Payment before Due.—The mere receiving of payment of a debt before it is due is not, in itself, proof of the existence of "reasonable cause to believe."

Sparker v. Marsh, 24 A. B. R. 280, 177 Fed. 739 (D. C. Ark.): "Great stress is laid on the fact that the payments to the bank and the defendant were made before the maturity of the notes. There is no evidence whatever to show that when the defendants received payment that they had any knowledge of the fact that the bank had been paid, but, even had they been advised of that fact, that alone would not have justified a finding that they had reasonable cause to believe the payment was intended as a preference. When White had the money to pay these debts, what would be more natural than that he should do so, especially, if by paying the note held by the defendants he saved the accumulated interest amounting to over \$50?"

However, such receiving of payment in advance under certain circumstances and taken in conjunction with other facts may be evidence of the existence of a reasonable cause for belief.⁵⁹

(Dissenting opinion) *Powell v. Gate City Bank*, 24 A. B. R. 316, 178 Fed. 609 (C. C. A. Mo.): "I shall not attempt an analysis of the proof. It manifestly created grave suspicion in the minds of the majority touching the good faith of the bank, but I think it went further. It is not very material whether the notes held by the bank were on their face payable in 90 days as claimed by the trustee, or whether they were on their face payable on demand as claimed by the bank. The fact is unquestionable that they were discounted for 90 days. The bank collected the interest on them in advance for that period of time. It entered them in its books as payable at the expiration of 90 days only. I cannot avoid the conclusion that whatever, the writing said, the parties, both the Humes Company and the bank, actually understood that the notes were not to be paid until the expiration of 90 days after their several dates. That time had not expired as to any of the notes on June 24th. The sudden call for their payment contrary to the understanding indicates something to my mind. Intelligent people generally act with a motive and for a purpose, and this is particularly true I think with respect to bank officials. They are anxious to loan their money at profitable rates of interest to responsible parties; and to keep it loaned, up to the full permissible legal limit. They are also especially keen and quick to follow up suspicion which points to probable loss. This, it is conceded, had been aroused in this case. With this condition of things as a background it is difficult to conceive why the Gate City Bank should have required the Humes Company to pay off a loan in advance of its actual maturity, especially so when it necessitated the refunding of money already collected by

⁵⁹. Compare *Shale v. Farmers' Bank*, 25 A. B. R. 888 (Sup. Ct. Kans.), quoted at § 1399.

way of discount, unless it believed it would be dangerous to leave its money with the company longer.

"It will avail nothing to discuss the testimony further. Suffice it to say that in my opinion all the facts and circumstances surrounding the payment of the money to the bank pointed strongly one way, and were entirely sufficient to lead an ordinary prudent business man to conclude that a preference was intended. Such being the case, the bank under all the authorities had reasonable cause to believe the Humes Company intended to give it a preference by such payment."

§ 1409. Failure to Investigate No Excuse Where Facts Sufficient to Put on Inquiry.—Failure actually to investigate will not excuse where the creditor's information was sufficient to have put the ordinary business man upon inquiry.⁶⁰

In *re McDonald & Sons*, 24 A. B. R. 446, 178 Fed. 487 (D. C. S. Car.): "Actual knowledge is not made the criterion of proof in such cases, nor is it necessary that it should appear that the bank actually believed that the mortgagor was insolvent, but the true inquiry is whether Mr. Mullins, as president of the bank, a lawyer, and business man of ordinary prudence, sagacity, and discretion, had reasonable cause to believe that the debtor was insolvent, in view of all the facts and circumstances, and, as it appears that the debtor was in fact insolvent, it seems to me clear that the circumstances were such as would put a person of ordinary prudence and discretion upon inquiry, and that it was his duty to make all such reasonable inquiry, and that there were such means of knowledge as would have enabled him to ascertain the true state of the case. A creditor, under these circumstances, is required to exercise ordinary prudence, and, if they failed to investigate, they are chargeable with all the knowledge which it is reasonable to suppose they would have acquired if they had performed their duty in that regard. Positive proof of collusion between debtor and creditor, by which one may be preferred, is not generally to be expected, and for that reason, among others, the law allows a resort to circumstances as the means of ascertaining the truth, and the rule of evidence is well settled that circumstances inconclusive if separately considered may by their joint operation, especially when corroborated by moral coincidences, be sufficient. Signs of insolvency were too many

60. *Crandall v. Coats*, 13 A. B. R. 712, 133 Fed. 965 (D. C. Iowa); In *re Eggert*, 4 A. B. R. 456, 457, 102 Fed. 735 (C. C. A. Wis.). Compare, to same effect, note in In *re Jacobs*, 1 A. B. R. 518 (D. C. La.). Compare, to same effect, In *re Pease*, 12 A. B. R. 66 (D. C. Mich.). Compare, also, to same effect, In *re Andrews*, 14 A. B. R. 247, 135 Fed. 599 (D. C. Mass.). Compare, to same effect, in fraudulent conveyance case, In *re Moody*, 14 A. B. R. 276, 134 Fed. 628 (D. C. Iowa). Compare, to same effect, obiter, *McMurtrey v. Smith*, 15 A. B. R. 435, 142 Fed. 853 (Spec. Master Approved by D. J.). Apparently contra, *Suffel v. Nat'l Bk.*, 16 A. B. R. 262 (Wis.), 106 N. W. 837. In *re Mills Co.*, 20 A. B. R. 501, 162 Fed. 42 (D. C. N. Car.); *Wright v. Skinner Mfg. Co.*, 20 A. B. R. 527, 162 Fed. 315 (C. C. A. N. Y.); In *re Tindal*, 18 A. B.

R. 773, 155 Fed. 456 (D. C. S. Car.); *Stephens v. Oscar Holway Co.*, 19 A. B. R. 399, 156 Fed. 90 (D. C. Me.); (1867) *Burfee v. First Nat'l Bk.*, 9 N. B. Reg. 314; *Rogers v. Fidelity Sav. Bk. & Loan Co.*, 23 A. B. R. 1, 172 Fed. 735 (D. C. Ark.); *Walters v. Zimmerman*, 30 A. B. R. 776, 208 Fed. 62 (D. C. Ohio); *Herron v. Moore*, 31 A. B. R. 221, 208 Fed. 134 (C. C. A. Cal.); *McGirr v. Humphreys*, 26 A. B. R. 518, 192 Fed. 55 (D. C. Ohio); *Coleman v. Decatur Egg Case Co.*, 26 A. B. R. 249, 186 Fed. 136 (C. C. A. Mo.), quoted at § 1399; *Gering v. Leyda*, 26 A. B. R. 137, 186 Fed. 110 (C. C. A. Neb.); *Spencer v. Nekemoto*, 24 A. B. R. 517 (D. C. Hawaii).

Instance where facts held not sufficient to require further investigation by creditor. *Newman v. Dry Goods Co.*, 31 A. B. R. 399 (Kansas City Court of Appeals), quoted at § 1407.

and too marked not to warn the president of this bank that he was getting a prohibited advantage over other creditors. The facts are so persuasive that they would have given reasonable ground for suspicion to persons far less astute and less accustomed to the ways of business in general than was the president of this bank. The unusual nature of the transaction, in connection with all the circumstances, raises such a presumption that it can only be overcome by proof on the part of the preferred creditor that he took the proper steps to find out the pecuniary condition of the debtor. Mr. Mullins has not testified in the case, nor has anyone in behalf of the bank testified as to its knowledge of the pecuniary condition of the bankrupts, or that they made any inquiries concerning it."

Collett v. Bronx Nat. Bank, 29 A. B. R. 454, 200 Fed. 111 (D. C. N. Y.): "Here the bankrupt at the time of giving a preference was confined in jail, and, probably fearing prosecution on a charge of converting a sum of money left with him for deposit in the bank, hastened to make restitution through the instrumentality of the cashier, his debtor, by satisfying the promissory notes which the bank held against him. Various officers of the bank knew of his dilemma. The cashier had full information regarding the accusation, and was probably aware of the bankrupt's financial condition. In any event, it appears that, in obedience to a telephone message from the bankrupt after his apprehension, the cashier discharged his obligations to the former by complying with his request to pay to the bank the amount owed by the cashier to the bankrupt.

"Under such circumstances, the defendant must be deemed to have had reasonable cause to believe that it was receiving a preference. The debt was paid under circumstances which put it upon inquiry and prompted investigation of the bankrupt's financial condition and the intention with which the indebtedness was satisfied. In *re McDonald* (D. C., S. C.), 24 Am. B. R. 446, 178 Fed. 487; In *re Leader* (D. C., Ark.), 26 Am. B. R. 668, 190 Fed. 624. Nothing was done by either the bank or its officers towards making an investigation, and the presumption is warranted that by the payment to the bank of its indebtedness against the bankrupt a preference was intended, and that the defendant had reasonable cause to believe such was the intention."

Hewitt v. Boston Strawboard Co., 31 A. B. R. 652 (Mass.): "If he prefers to draw inferences favorable to himself, and to ignore information which would have led to knowledge that his debtor was in failing circumstances, he can not set up his own judgment to the contrary, even if honestly entertained, as a reason why he should be permitted to retain a prohibited advantage."

In *re Herman*, 31 A. B. R. 243, 207 Fed. 594 (D. C. Iowa): "The fact that no part of the prior loan had been paid, though it was then nine months past due, with the request for an additional loan of \$500 to carry him over until fall, was sufficient to put her as a reasonably prudent person upon inquiry as to his then financial condition; and she was then chargeable with all the information that such an inquiry would have disclosed. If such inquiry had then been made, there can be no doubt that it would have disclosed that the bankrupt was hopelessly insolvent, that he was being pressed by the bank for the payment of its debt, that he was unable to do so, and that the mortgage was intended as a preference to Mrs. Crocker over the bank and other creditors of the bankrupt.

"Again, Mrs. Herman acted for her mother in requiring the promise that a mortgage should be given by the bankrupt when the last loan was made (if it was made) and when the mortgage was recorded it was delivered to her to be forwarded to her mother. To hold that she had no reasonable grounds to believe, when she so received and forwarded the mortgage, that it was intended

as a preference to her mother, would be to disregard the testimony and sanction a deliberate violation of the Bankruptcy Act."

Lazarus v. Egan, 30 A. B. R. 287, 206 Fed. 518 (D. C. Pa.): "I can not excuse the conduct of Eagan because of the advice of counsel, representing as well the bankrupt. The facts necessary to disclose the bankrupt's true financial situation were within his own reach and I can not be made to believe that he having lived across the street in a small town, known the bankrupt for many years, and a director of the bank in which he was endorser and kept his accounts, was ignorant of them. If he was, he remained so willingly, and the law will not let him profit."

In re Dorr, 28 A. B. R. 505, 196 Fed. 292 (C. C. A. Cal.): "It is true that the mere fact that the bankrupt had no money on deposit at Los Angeles was no indication that he was unable to meet his obligations, for the money might well have been on deposit in one or more of the many other banks in which he carried his accounts. But the fact, if such had been the fact, that the money was deposited in other banks, would not have prevented its immediate transfer to Los Angeles, for the evidence shows, and it is not disputed, that this could have been done 'by wire instantly.' Another fact is that when, on July 7th, the appellant was informed that the money could not be paid him, he still demanded checks for the full sum of \$40,000, and on the following day, when he found that the bankrupt could pay him but \$14,000, he demanded and received a further check for \$26,000, although he knew that the check was drawn on a bank in which there were no funds available for its payment, and that on the following day he would have to return that check and receive others in lieu thereof. In short, he was advised of the desperate financial straits of the bankrupt, and we would not be justified in holding that the referee and the court below erred in holding that he was put upon inquiry to ascertain whether or not the bankrupt was solvent."

Rogers v. Page, 15 A. B. R. 505 (C. C. A. Tenn.): "Thos. Merriam was aware of his brother's condition at the time he bought the land here involved or of such suspicious facts as to charge him with inquiry and notice of such facts as he might have learned by inquiry conducted in good faith."

McElvain v. Hardesty, 22 A. B. R. 320, 169 Fed. 31 (C. C. A. Mo.): "Moreover, if McElvain did not have actual knowledge of the insolvent condition of his debtors, we think in the circumstances of this case he is constructively chargeable with that knowledge. He took a transfer of all his debtors' property—of a going concern—in satisfaction of a debt. This in itself was an unusual thing, and the reasons which actuated it must have sprung from a fear or suspicion of danger. Solvent and prosperous business houses do not commonly pay debts that way. He knew of his own dishonored notes. He knew that his debtors could not have carried on active business for seven months and thereby make enough to pay over \$2,600 upon his own indebtedness, assumed by them, without purchasing supplies. These facts and many others disclosed by the record were sufficient to put him as an ordinarily prudent man upon inquiry as to his debtor's solvency and to charge him with all the knowledge he could have acquired by the exercise of reasonable diligence."

Plate Glass Co. v. Edwards, 17 A. B. R. 447, 148 Fed. 377 (C. C. A. Iowa): "He testified to efforts to ascertain the bankrupt's financial condition, whether he owed certain parties, and that he relied on the information obtained, but he ignored other sources of information which were at hand and were so obvious and so much more accurate and reliable that in view of the undisputed facts of the case intentional avoidance is suggested."

In re Nassau, 14 A. B. R. 828, 140 Fed. 912 (D. C. Pa.): "The circumstances accompanying the transaction were such as to put the mortgagee's agent upon inquiry, and it can scarcely be doubted that very slight investigation would have led to knowledge of the bankrupt's financial condition."

Brewster v. Goff Lumber Co., 21 A. B. R. 106, 164 Fed. 124 (D. C. Pa.): "But the trustee must go further, to make out a case, and show that the Goffs had reasonable cause to believe that they were getting a preference; and this depends on whether they might or ought to have known, that Moore & Son were insolvent, as to which they were affected with whatever put them on inquiry and would lead to a disclosure, actual knowledge not being required."

Coder v. McPherson, 18 A. B. R. 523, 152 Fed. 951 (C. C. A. Iowa): "Notice of facts which would incite a man of ordinary prudence to an inquiry under similar circumstances is notice of all the facts which a reasonably diligent inquiry would disclose. The bank knew that Armstrong had stated that he owed only \$36,000 in December, 1903, that he had given a mortgage to Arts for \$98,503.32 in May, 1904, and that he had stated on June 13, 1904, that he owed \$147,500 secured by mortgages upon his lands and \$47,900 that was unsecured. According to these two statements which he had given to the bank, his indebtedness had increased \$159,400 between December 24, 1903, and June 13, 1904, and his assets less than \$9,000. Two such statements would inevitably incite the ordinary creditor to inquire what had become of the \$150,000 which the increased indebtedness indicated that the debtor had received and had not added to his property during these six months, and such an inquest would have developed the fact at once that Armstrong's statements were not true."

Thus, careful abstinence from making inquiries as to financial condition, when the transfer, which itself is out of the ordinary course of trade, is made, will tend to prove cause for belief.⁶¹ And if the debtor is known to be insolvent it would seem the creditor is bound to exercise ordinary prudence and diligence to ascertain whether or not such insolvent can make a transfer that will not be in violation of the Bankruptcy Act;⁶² and, under such circumstances, if the transfer is out of the usual and ordinary course of trade, it will tend to negative good faith.⁶³

But the rule charging the creditor with knowledge must have a reasonable construction, and to make it operate justly must relate to information concerning the financial condition and property of the debtor.⁶⁴ But it has been held, though the ruling is doubtful and the opposite rule, if anything, more reasonable, that a higher degree of proof is requisite than in cases of fraudulent conveyances.

61. Huttig Mfg. Co. v. Edwards, 20 A. B. R. 349, 160 Fed. 619 (C. C. A. Iowa).

62. Analogously, as to fraudulent conveyance, In re Moody, 14 A. B. R. 272, 134 Fed. 628 (D. C. Iowa).

63. Analogously, In re Moody, 14 A. B. R. 272, 134 Fed. 628 (D. C. Iowa); Walburn v. Babbitt, 16 Wall. 577; Toof v. Martin, 13 Wall. 40.

Inferentially, In re Butler, 9 A. B.

R. 539, 120 Fed. 100 (D. C. Mass.): In this case the court held that the mortgage was out of the ordinary course of the business of the bankrupt, because he was a retail dealer, doing business of about \$100 a day, and a mortgage of such a trader's full stock is an open confession of insolvency. Citing Nary v. Merrill, 8 Allen 451.

64. In re Pfaffinger, 18 A. B. R. 807, 154 Fed. 528 (D. C. Ky.), quoted at § 1399.

Suffel v. Nat'l Bk., 16 A. B. R. 262, 106 N. W. (Wis.) 837: "The obvious meaning of this language when construed in connection with the other findings mentioned, is that the court held, as a matter of law, that the present Bankrupt Act does not require the same diligence of creditors concerning preferential payments, that is required of grantees in cases of fraudulent conveyances; and hence, that the facts known to the cashier at the time of receiving the payment, though sufficient to produce in his mind a doubt or suspicion of Dickinson's solvency, yet that they were insufficient to prove that the cashier had at the time reasonable cause to believe that Dickinson was then insolvent or that in making such payment he intended to give a preference to the defendant. This is in harmony with the conclusion of the lengthy opinion of the trial judge, where he said, in effect, that the point to be decided was somewhat difficult, but a considerable reflection had led him to the conclusion that the knowledge of facts and circumstances possessed by the cashier, were well calculated to produce a doubt or raise a suspicion in the mind of an ordinarily intelligent man, as to Dickinson's solvency, but not such as was calculated to produce a belief of it; and as that was essential to the plaintiff's cause of action, he could not recover."

And higher, even, than under the old law of 1867, where insolvency had a different meaning, and consequently, also, reasonable cause for belief of a preference had a different meaning.⁶⁵

The doctrine that the creditor is chargeable with such facts as he would have discovered by investigation where the facts actually known to him were sufficient to put him on inquiry is rejected in some cases.⁶⁶

Where facts are sufficient to put a creditor on inquiry, yet if thereupon such creditor does properly make inquiry and fails to ascertain facts that would indicate a deficiency of assets to meet obligations, it would seem that then the creditor is excused.⁶⁷

Where a debtor has not enough money to carry out a settlement made on an equal percentage with all creditors, it is exacting too great a diligence to require the creditors receiving their shares to investigate the ability of the debtor to pay the others their respective shares likewise.⁶⁸

§ 1410. Date of Recording, Date for Existence of Reasonable Cause of Belief.—Even before the Amendment of 1910, if since the Amendment of 1903, it was probably the true rule that in cases where the transfer was effected by an instrument requiring record by State law to make it effective as against levying creditors, the date of such recording was the date at which the existence of such reasonable cause for belief was to be proved, such being the date of the effective transfer as against other creditors.⁶⁹

⁶⁵. In *re* Pettingill & Co., 14 A. B. R. 758 (in note), 135 Fed. 220 (C. C. A. Mass.); *Suffel v. Nat'l Bk.*, 16 A. B. R. 259, 106 N. W. (Wis.) 837; In *re* Andrews, 16 A. B. R. 392 (C. C. A. Mass.).

⁶⁶. *Stuart v. Farmers' Bk. of Cuba City*, 21 A. B. R. 403, 137 Wis. 66, 117 N. W. 820.

⁶⁷. In *re* Bartlett, 22 A. B. R. 891, 172 Fed. 679 (D. C. Pa.), quoted at § 1402.

⁶⁸. *Smith v. Hewlett Robin Co.*, 24 A. B. R. 153, 178 Fed. 271 (C. C. A. N. Y.).

⁶⁹. See ante, § 1379½. And compare *Carey v. Donohue*, 31 A. B. R. 210, 209 Fed. 338 (C. C. A. Ohio).

McElvain v. Hardesty, 22 A. B. R. 320, 169 Fed. 31 (C. C. A. Mo.): "As, for the purposes of this case, the transfer is to be treated as made on the date the agreement was recorded, so the transferee's belief or cause for belief concerning it must relate to that time. The evidence of two witnesses, including Carter, one of the firm, strongly tends to show that McElvain had full knowledge of the hopelessly insolvent financial condition of the firm when he recorded the agreement and took possession of the saloon."

Amendment of 1910.—But by the Amendment of 1910 to Bankr. Act § 60 (b) the question has been put at rest: the date of the recording is the date at which the "reasonable cause" must be proved to have existed.⁷⁰

§ 1411. **Cause for Belief Not Necessarily That of Person Receiving—May Be That of Person Benefited.**—The reasonable cause for belief need not be on the part of the one actually receiving the preference, but may be either on the part of the one actually receiving it, or on the part of the one benefited by the preference.⁷¹ This rule is particularly applicable to indorsers, etc., upon commercial paper.⁷²

§ 1411½. **As, for Instance, Endorsers and Others Secondarily Liable.**—Reasonable cause for belief on the part of an endorser or other person secondarily liable is sufficient to charge endorser or other person with the receipt of a voidable preference even though the actual transfer was made to the holder.⁷³

And, of course, where the recovery sought is from the person benefited then the person benefited must be proved to have had the reasonable cause of belief; as, for example, where recovery is sought from an accommodation endorser for the bankrupt, it is essential to prove the existence of the reasonable cause of belief on the part of the endorser.⁷⁴

§ 1412. **Agent's Knowledge Imputed to Principal.**—Knowledge of an agent engaged in the transaction, or the existence of a reasonable cause

70. Bankr. Act, § 60 (b), as amended 1910, quoted ante, § 1334½. Also, see ante, § 1379½. Compare, *Carey v. Donohue*, 31 A. B. R. 210, 209 Fed. 328 (C. C. A. Ohio).

71. Bankr. Act, § 60 (b); compare *Swarts v. Siegel*, 8 A. B. R. 220, 117 Fed. 113 (C. C. A. Mo.). Also, *Swarts v. Fourth Nat'l Bk.*, 8 A. B. R. 673, 117 Fed. 1; *Landry v. Andrews*, 6 A. B. R. 281, 48 Atl. 1036 (Sup. Ct. R. I.). Compare, inferentially, to same effect, *Western Tie & Timber Co. v. Brown*, 12 A. B. R. 111, 129 Fed. 728 (C. C. A. Ark., reversed 13 A. B. R. 447, 196 U. S. 502); compare, *In re Sanderson*, 17 A. B. R. 875 (D. C. Vt.).

Assumed to be the law but facts held insufficient. *Sparks v. Marsh*, 24 A. B. R. 280, 177 Fed. 739 (D. C. Ark.).

72. *Reber v. Shulman & Bro.*, 24 A. B. R. 782, 179 Fed. 574 (D. C. Pa.),

affirmed 25 A. B. R. 475, 183 Fed. 564 (C. C. A. Pa.).

Compare, where facts held insufficient to show that the president of a bankrupt corporation had caused it to make the transfer in order to relieve him from his endorsement. *Page v. Moore*, 24 A. B. R. 745, 179 Fed. 988 (D. C. Pa.).

73. See cases cited at § 1411. Conceded as the law though facts held insufficient to charge such endorser with such reasonable cause of belief. *Reber v. Shulman & Bro.*, 24 A. B. R. 782, 179 Fed. 574 (D. C. Pa.), affirmed 25 A. B. R. 475, 183 Fed. 564 (C. C. A.); *Sparks v. Marsh*, 24 A. B. R. 280, 177 Fed. 739 (D. C. Ark.).

74. *Reber v. Shulman*, 24 A. B. R. 782, 179 Fed. 574 (D. C. Pa.), affirmed 25 A. B. R. 475, 183 Fed. 564 (C. C. A.).

for his believing, is to be imputed to the principal.⁷⁵

Hewitt v. Boston Strawboard Co., 31 A. B. R. 652, 214 Mass. 260: "By the express words of the Amendatory act which are merely declaratory of the rule of law that knowledge possessed by an agent may be imputed to his principal, the defendant is bound by the information obtained by the attorney who made the attachment, and acted for it in effecting the settlement."

Collett v. Bronx National Bank, 30 A. B. R. 599, 205 Fed. 370 (C. C. A. N. Y.): "We think that the knowledge which Kolbe, as cashier of the defendant, had November 16th, viz, that Belling had borrowed money on a forged certificate of the bank's stock and was unwilling to make any explanation, was imputable to the bank, and that it constituted reasonable cause to believe that Belling was insolvent. Such an act, and such conduct following it, are the clearest evidence of ruin and desperation. When, on the next day, Kolbe, at Belling's request, applied \$1,250 of his indebtedness to Belling on account of Belling's indebtedness to the bank, it followed that the bank had reasonable cause to believe that such payment would give it a preference."

Thus, where a bank receives a note for collection and acts as a mere conduit through which a direct connection is made with the owner or collector, a privity exists, and the collecting bank will be deemed to be the agent of the owner, so that the owner will be chargeable with knowledge of such facts as were known to his collector. On the other hand, however, if the collecting bank acts as an independent contractor in making the collection, no privity exists between it and the owner; nor, in such case, will the owner be chargeable with knowledge of facts known to the collecting bank.⁷⁶

But this information must have been obtained by the agent acting in the premises.⁷⁷

Constam v. Haley, 30 A. B. R. 650, 206 Fed. 260 (C. C. A. Tenn.): "Constam lived in Baltimore. He had purchased the note from Schloss Bros. & Co. the payees. After the maturity and nonpayment of his note he gave it to Schloss Bros. & Co., and they intrusted it to Caston, their 'credit man,' to take to Chattanooga, where the debtor was in business, and to collect or adjust. Caston's Chattanooga trip was, primarily, in the interest of his regular employer, but he was at the same time in this transaction authorized to represent and act for Con-

⁷⁵. *In re Teague*, 2 A. B. R. 168 (D. C. Ind.); *In re Dubant*, 3 A. B. R. 42, 96 Fed. 542 (D. C. N. Car.); *In re Nassau*, 14 A. B. R. 828, 140 Fed. 912 (D. C. Penn.), affirming 15 A. B. R. 793; *Campbell v. Balcomb*, 25 A. B. R. 538, 183 Fed. 766 (C. C. A. Ills.); *Painter v. Township of Napoleon*, 26 A. B. R. 324, 190 Fed. 637 (D. C. Ohio).

Inferentially, *In re Wright Lumber Co.*, 8 A. B. R. 345 (D. C. Ark.): This case, however, was a case of surrender of an "innocent" preference as a prerequisite to sharing in the dividends before the Amendment of 1903. Compare, inferentially, *In re Beerman*, 7 A. B. R. 431, 112 Fed. 663 (D. C. Ga.).

Instance, *Brewster v. Goff*, 21 A. B. R. 239, 164 Fed. 127 (D. C. Pa.); in-

stance, bank acting as lender's agent in procuring loan to be used in preferring the bank itself, *In re Lynden Mercantile Co.*, 19 A. B. R. 444, 156 Fed. 713 (D. C. Wash.).

[Bankrupt, was general business manager of creditor corporation and paid the bookkeeper; bankrupt's knowledge imputed to corporation creditor.] *Rogers v. American Halibut Co.*, 31 A. B. R. 576 (Mass.), quoted at § 1413.

⁷⁶. *Balcomb v. Old Nat. Bank*, 29 A. B. R. 329, 201 Fed. 679 (Wis.).

⁷⁷. Bankr. Act, § 60 (b). "* * * or his agent acting therein * * *." See, also, *Blackburn v. Vigors* [Eng.], L. R. 12 App. Cas. 531.

stam. Caston's activity resulted in the making, at that time or shortly afterwards, of the first two or three of the payments now in question. We think it fairly inferable from all the facts and circumstances which it would be unprofitable to recount that Caston, on this occasion, learned enough of the actual situation to give him reasonable cause to believe that insolvency existed. * * * In the instant case Caston's employment and duty were relatively general in scope. It was his duty to do whatever was for Constam's interest, and to acquire and communicate to Constam all he could learn about the debtor's pecuniary condition."

Babbit v. Kelly, 9 A. B. R. 335 (Court of App. at St. Louis, 70 S. W. 384): "Knowledge by an agent of a creditor, or the agent's reasonable cause to believe, that a debtor is insolvent when he does a preferential act in favor of the agent's principal, affects the latter."

§ 1413. Except When Agent Acting for Own Interest.—But, of course, the knowledge of the agent is not the knowledge of the principal when the agent is acting in his own interest.⁷⁸

Obiter, *Rogers v. American Halibut Company*, 31 A. B. R. 576 (Mass. Sup. Jud. Court): "By § 60b, knowledge possessed by his agent binds the creditor, but this provision is to be taken with the qualification that where the agent is acting in furtherance of his own adverse interest or fraudulently his principal is not bound."

At least, when he is acting solely in his own interest; or when he had acquired the knowledge while acting as attorney for the bankrupt.

And it has been held that where a creditor's attorney has, later, been employed by the bankrupts and, on the morning of the day on which they file their petition and schedules in bankruptcy, receives collection of the creditor's claim in full and straightway turns it over to his client, the attorney himself, in the absence of fraud, may not be charged with the amount, but the trustee must pursue the client.⁷⁹

In re Martin & Co., 29 A. B. R. 705, 167 Fed. 236 (D. C. N. Y.): "The theory of the special commissioner is that, Mr. Turk being aware of the bankrupts' financial condition when he made the payment, it should therefore be regarded as a nullity, and he should be required to pay the money involved into the estate. The theory of Mr. Turk is that he merely acted as agent in the matter, and if there is to be any recovery of the money, recourse to Mr. Paris, the principal, should be had. I think the contention of Mr. Turk should be sustained. No doubt the knowledge which an agent obtains is, under ordinary circumstances, often imputable to his principal, but a somewhat different rule applies where the relations of attorney and client are involved and there is no question of fraud. In the latter case it is the duty of an attorney to turn a collection, made in the ordinary course of business, over to his client and not to a third person. This matter has not been litigated upon any theory

⁷⁸. *Crooks v. Bk.*, 5 A. B. R. 754 (N. Y. Sup. Ct.): In this case the president of the bank alleged to be guilty of receiving the preference was also the leading member of the debtor firm. *In re Ebert*, 1 A. B. R. 340 (Ref. Wis.); *Benner v. Blumauer-Frank*

Drug Co., 28 A. B. R. 798, 198 Fed. 362 (D. C. Wash.); *Painter v. Township of Napoleon*, 26 A. B. R. 324, 190 Fed. 637 (D. C. Ohio), quoted at § 1414.

⁷⁹. Compare post, § 1821½.

of fraud, in which event, a fraud being established, a more stringent rule against the attorney should be applied (*Mayer v. Herman*, 16 Fed. Cas. No. 1,241. Here an order for the payment of money was made against an attorney who collected the sum in pursuance of business committed to him long before the bankruptcy, and who paid it in due course to his client. It seems to me that compelling the attorney to pay the amount again is not justified, and the referee's order to that effect should not be sustained."

Doubtless a different rule would prevail in case fraud were involved.

Where the president of one corporation stole from it and put the money into another corporation and later stole from the latter corporation and replaced the money taken from the first corporation, without the knowledge of the original victim, it was held not to be a preference, because of the nonexistence of "reasonable cause for belief."⁸⁰ It would seem that several other elements also were lacking—for instance, voluntary action of the corporation from whom the money was last stolen was lacking, hence there was no "transfer;" likewise, it is questionable whether there was a depletion of the assets of the last corporation since the money taken from it was stolen money.

However, where the bankrupt in making the transfer claimed to be preferential is also "then acting therein" for the creditor receiving the transfer, his knowledge is imputable to his principal.

Clarke v. Rogers, 228 U. S. 534, 30 A. B. R. 39: "As we have said, there may be a unity of the person in the individual and the trustee, of the individual and the guardian; we must look beyond it to the difference in his capacities and the duties and obligations resulting from it. These duties and obligations are as distinct and insistent as though exercised by different individuals, and have the same legal consequences. The unity of the person has, of course, an effect. It constitutes such relationship between the different capacities exercised as to impute knowledge of their exercise and for what purpose exercised."

Similarly, where the managing officer of the bankrupt company made payments to himself as a creditor out of the funds of the company.

Cooper v. Miller, 30 A. B. R. 194, 203 Fed. 383 (C. C. A. Ky.): "While the intent of the company is not by reason of the amendment, important here, yet the company was chargeable with the knowledge of its president, and both the company and Miller must have known that the debtor could not pay its other creditors a percentage of their claims similar to the rate he was paying himself, and, consequently, that the enforcement of the transfer would inevitably give to him a preference over the other creditors of the same class. * * * The dual relation of Miller to the company, as its official head and as creditor, we think, justifies the inference that his admissions of the company's insolvent condition meant that he understood the fair value of its property to be less than its debts."

But the fact that the agent and the insolvent have confidential relations;

⁸⁰. *McNaboe v. Columbian Mfg. Co.*, 18 A. B. R. 684, 153 Fed. 967 (C. C. A. N. Y.).

or that the agent's self-interests are antagonistic to those of his principal, will not render the transaction any the less preferential.

Campbell v. Balcomb, 25 A. B. R. 538, 183 Fed. 766 (C. C. A. Ills.): "The statute purports to give the whole law on the subject. In it we find no exceptions to the effect that a preferred creditor may hold his advantage provided his agent and the insolvent have confidential relations, or provided his agent has self-interests antagonistic to a disclosure to his principal. To interpolate such exceptions we deem beyond the proper sphere of statutory construction and violative of the spirit of the act wherein equality of distribution of the bankrupt's inadequate assets is a prime object."

Thus, where the bankrupt had made a mortgage to the president of a bank to which he owed money, with the proceeds of which the bankrupt paid his debt to the bank, the knowledge of the president was imputed to the bank.⁸¹

§ 1414. Whether Public Corporations Chargeable with "Reasonable Cause for Believing."—It is a question whether a public corporation can be charged with participation in the preferential intent, it not being bound by tortious acts of its agents.⁸² But the exemption only applies to its governmental functions, and it would seem that the same rules should apply to public corporations as to other creditors.

Painter v. Napoleon Township, 19 A. B. R. 412, 156 Fed. 289 (D. C. Ohio): "The recitals of the bill indicate that the pleader intended to cover violations of § 60a and § 60b, Bankruptcy Act,— * * * as amended by act, Feb. 5, 1903, * * * and § 67e of the Bankrupt Act. By the Act of 1903 amending §§ 23b, 60b, and 70e, a trustee in bankruptcy is authorized to bring a suit to recover property. This is not an action for personal injury arising from the negligent act of omission or commission on the part of the township's agents, but an action authorized by the national bankrupt law to recover money charged to have been paid to the board of township trustees by Delventhal, while insolvent, within five days prior to his adjudication as a bankrupt, with an intent to create a preference and to defraud his other creditors, and to have been received by the board with reason on its part to believe and know that he was insolvent at the time of payment, and that the payment was purposely made to prefer the township as a creditor. If the averments of the bill are true, and if the effect of the payment to the board of trustees was to enable it to obtain a greater percentage of its debt than any other creditor of the same class, then Delventhal's property, in the distribution of which his creditors are entitled to share, was wrongfully, and in violation of the provisions of the Bankrupt Act received and appropriated by the board of trustees to the use and benefit of the township, and the board now seeks to retain and enjoy the benefits thus obtained by its own wrongful act. The nature of the bankrupt's liability to the township is not stated, nor is there a showing of when and how such liability arose; but, if the board's contention is correct, an insolvent debtor, within four months prior to the filing of a petition in bankruptcy, or after the filing of such petition and before the adjudication thereof, may designedly and successfully, with an intent to defraud his creditors, create a preference in favor of a township whose agents know or have reasonable cause

⁸¹ *Walters v. Zimmerman*, 30 A. B. R. 776, 208 Fed. 62 (D. C. Ohio).

⁸² *In re Shultz & Marks*, 11 A. B. R. 690 (Ref. N. Y.).

to believe and know that a preference in its behalf is intended, and that the enforcement of such transfer will be to enable it to obtain a greater percentage of its debt than any other of the bankrupt's creditors of the same class. The township would thereby obtain and retain a greater percentage of its debt than any other creditor of the same class, and thus defeat the salutary provisions of a beneficent law designed to accomplish an equitable distribution among creditors of bankrupt estates. In *Marsh v. Fulton County*, 10 Wall. 676, 19 L. Ed. 1040, Mr. Justice Field said: 'The obligation to do justice rests upon all persons, natural and artificial, and, if a county obtains the money or property of others without authority, the law, independent of any statute, will compel restitution or compensation.' The same obligation in this respect rests upon a township as upon a county. The rights and remedies of a trustee in bankruptcy are created and defined by Congress, which, under the federal Constitution (article 1, § 8, cl. 4), has exclusive control of the subject of bankruptcies, with the one qualification that its laws thereon shall be uniform throughout the United States. The rights given and the remedies thus created by federal statute may be enforced against townships or their boards of trustees. Nor is the State's permission, by legislative enactment or otherwise, necessary to the maintenance of an action of this character, or to make townships or their boards of trustees liable therein. Had the Legislature of Ohio specially enacted that townships and their boards of trustees should be exempt from liability in cases like this, such enactment would be ineffective. *Bliss v. City of Brooklyn*, 30 Fed. 250; *May v. County of Ralls* (C. C.), 31 Fed. 473. If a State law conflicts with an act of Congress, the State law must yield (*Smith v. Parsons*, 1 Ohio, 236, 13 Am. Dec. 608), because the laws of the United States, when made in pursuance of the Constitution, form the supreme law of the land, anything in the Constitution or laws of the State to the contrary notwithstanding (*McCulloch v. Maryland*, 4 Wheat. 316, 4 L. Ed. 579; article 6, Const. U. S.; *In re Debs*, 158 U. S. 564, 579, 15 Sup. Ct. 900, 39 L. Ed. 1092; *Lewis' Sutherland's Stat. Constr.* [2d Ed.] 22)."

Painter v. Township of Napoleon, 26 A. B. R. 324, 190 Fed. 637 (D. C. Ohio): "To say that Napoleon Township did not know of the insolvency of Henry Delventhal and did not know of his indebtedness to it and could not know it until the trustees were convened in session is to state a proposition that we are sure no reasonable person would adhere to, and yet, in the ultimate, that is the proposition involved in the claim that the township had no reasonable cause to know the results of this situation because the facts were known to one member of the board only. If they were known to William Delventhal officially, then, surely, they were known to the township. If we may say that they were known to William Delventhal unofficially only, then we reach the absurd conclusion that if they were known unofficially or in the same way to each of the three individual members of the board of trustees, the township could not be charged with knowledge until these three gravely got together and resolved that their unofficial knowledge should become public."

And knowledge of one of the township trustees who was a brother of the debtor has been held sufficient to bind the township.⁸³

§ 1415. Whether Purchaser at Trustee's Sale Entitled to Set Aside Preferential Encumbrances on Property Purchased.—A pur-

⁸³. *Painter v. Township of Napoleon*, 26 A. B. R. 324, 190 Fed. 637 (D. C. Ohio), quoted supra, § 1414.

chaser of property from the trustee, or of the trustee's interest in property, at judicial sale has been held entitled to set aside preferential encumbrances upon the property or other preferential transfers of it precisely as would be the trustee himself.

Bryan v. Madden, 11 A. B. R. 763, 78 N. Y. Sup. 220: "If this action had been brought by the trustee his right to recover would have appeared to be clear. Instead of bringing an action, however, by order of the District Court he was directed to transfer the interest of the bankrupt to a purchaser upon a sale made by him which he did. * * * The intention and effect was to assign whatever right the trustee in bankruptcy had, and that right was the same as the one which the trustee himself could reach, for by the orders for the sale and the sale the trustee parted with every interest he had in the bankrupt's contracts. * * * So far as he undertakes to pass property rights he assigns all that he can assign, and it is a wholesome rule that he can dispose of property interests which may be the subject of litigation, allowing others interested to carry the burden."

But this ruling has been expressly disapproved.

Manufacturing Co. v. Lumber Co., 23 A. B. R. 595, 175 Fed. 335 (C. C. A. Mich.): "A conveyance of property by a bankrupt within four months before bankruptcy, which would be fraudulent at the common law, is a void conveyance under the sixty-seventh section of the bankruptcy law, and the title would vest in the bankrupt's trustee. But it is otherwise as to a conveyance which is a mere preference under § 60 of the same act, and would be merely voidable at the suit of the trustee. This is not a suit by the trustee, but by an assignee of the trustee. If the delivery was a preference, the trustee only could maintain a suit to avoid it. He may not transfer to another this right of avoidance. *Bryan v. Madden*, 15 Am. B. R. 388, 109 App. Div. 876, 96 N. Y. Supp. 465, has been cited to the contrary. We cannot agree to the conclusion of the Supreme Court of New York."

It has been held that whilst the naked right of action to set aside the transfer is not in itself assignable, yet it may pass to the purchaser as an incident to the sale of the trustee's interest in the property.

In *re Downing*, 27 A. B. R. 309, 199 Fed. 329 (D. C. N. Y.): "It seems to me that inasmuch as the trustee in bankruptcy was vested with all the right, remedies and powers of a judgment creditor of the bankrupt with execution returned unsatisfied, and one of those rights is (assuming the transfer was in fraud of creditors) to set aside the transfer, have the specific real property sold, or sell same, and the proceeds applied to the payment of all proved and allowed claims against the bankrupt, the trustee has an interest in such property. His rights and interest are something more than a mere possibility or expectancy, not coupled with any interest in or growing out of property. And it is something more than a litigious right. If the action is prosecuted successfully the judgment reaches and operates on the specific property sold or transferred by the bankrupt,—the title of the fraudulent vendee is divested,—and the true title transferred to a purchaser as to the trustee in bankruptcy and the proceeds so far as necessary go to the trustee for creditors or to the purchaser of such rights from such trustee. It is true that the transferee (assignee) of the trustee in bankruptcy would not be prosecuting the action for the benefit of the creditors of the bankrupt but in his own interest and for

his own benefit. The answer to this is that such assignee of the trustee has paid a consideration for the transfer of the rights to the trustee, who holds the same for the creditors."

It has also been held that such a purchaser may maintain suit in the trustee's name to set aside the fraudulent encumbrance.

In *re Downing*, 27 A. B. R. 309, 199 Fed. 329 (D. C. N. Y.): "I am compelled to hold that while the right of a trustee in bankruptcy to bring suit to set aside a deed as made in fraud of the creditors of the bankrupt may not alone be assigned, still a trustee in bankruptcy has a transferable interest in real estate owned by the bankrupt and transferred by him in fraud of his creditors more than four months before the institution of proceedings in bankruptcy against him, and that such trustee may transfer or convey same and assign with it the rights vested in him by statute to maintain an action to set aside such fraudulent transfer."

§ 1416. Right of Preferred Creditors to Offset New Credit.—If a creditor has been preferred, and afterwards, in good faith, gives the debtor further credit, without security of any kind, for property which becomes a part of the debtor's estate, the amount of such new credit remaining unpaid at the time of the adjudication in bankruptcy may be set off against the amount which would otherwise be recoverable from him.⁸⁴

Gans v. Ellison, 8 A. B. R. 153, 114 Fed. 734 (C. C. A. Pa.): "Upon the true interpretation of paragraph 'a' of § 60, the preference in such case as this is the net gain to the creditor upon the transactions between him and the debtor. The net balance in favor of the creditor is the real preference under the law. For only to the extent of such net gain does the creditor 'obtain a greater percentage of his debt than any other creditors of the same class.' And so, on the other hand, only to the amount of the net gain to the creditor is the estate of the debtor impaired. If, then, a creditor innocently preferred has given return credits afterwards he has surrendered his preference to the extent of such return credits. To effectuate justice, both sides of the account are to be considered in the case of a creditor who innocently has received preferences, and afterwards in good faith has given the debtor further credit without security, for property which has become a part of the debtor's estate. Otherwise it is plain that such innocently preferred creditor would be compelled to surrender his preference a second time before he could prove his claim against

⁸⁴. Bankr. Act, § 60 (c); *Kaufman v. Treadway*, 12 A. B. R. 683, 195 U. S. 271, quoted post, § 1423; *Peterson v. Nash*, 7 A. B. R. 181, 112 Fed. 311 (C. C. A. Minn.), quoted post, § 1418; *In re Christenson*, 4 A. B. R. 202, 101 Fed. 802 (D. C. Iowa); *In re Sodolsky*, 7 A. B. R. 123, 111 Fed. 511 (D. C. Minn.); *McKey v. Lea*, 5 A. B. R. 267, 195 Fed. 923 (C. C. Ills.); compare, *Kimball v. Rosenham Co.*, 7 A. B. R. 718, 114 Fed. 85 (C. C. A. Ark.); *In re Thompson's Sons*, 7 A. B. R. 214, 112 Fed. 651 (D. C. Penn.); *Kahn v. Export Co.*, 8 A. B. R. 157, 115 Fed.

290 (C. C. A. Ga.); impliedly, *In re Bullock*, 8 A. B. R. 646, 116 Fed. 667 (D. C. N. Car.); impliedly, *In re Sagar & Bro.*, 9 A. B. R. 361, 121 Fed. 658 (C. C. A. N. Y.); compare, *Carleton Dry Goods Co. v. Rogers*, 9 A. B. R. 787 (C. C. A. Tex.); *Price v. Derbyshire Coffee Co.*, 21 A. B. R. 280, 128 App. Div. 472, 112 N. Y. Supp. 830; compare, *In re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.); *In re Searles*, 29 A. B. R. 635, 200 Fed. 893 (D. C. N. Y.); *Rogers v. American Halibut Co.*, 31 A. B. R. 576 (Mass.).

the bankrupt's estate." Although this case was decided as to "innocent" preferences before the Amendment of 1903, the principles involved are the same.

§ 1417. **Right Distinguished from Offset under § 68.**—This is a different right from that referred to in § 68, relative to the preservation of the right of offset of mutual debits and credits.⁸⁵

§ 1418. **Basis of Right.**—The basis of the right of offset of new credits against previous preferences is the pro tanto enrichment of the trust fund, by the new property thrown into it after the previous depletion of it occasioned by the taking of the preference out of it.

The theory of thus allowing offset against preferences seems to be that the goods so furnished on credit after the preference, were contributions to the trust fund already belonging to creditors by virtue of the insolvency of the debtor; that correlatively to the right of all creditors to share as equal beneficiaries in the trust fund after the insolvency, is the right of a party to withdraw such subsequent contributions therefrom.⁸⁶

Jacquith v. Alden, 9 A. B. R. 773, 189 U. S. 78: "In the present case all the rubber was sold and delivered after the bankrupt's property had actually become insufficient to pay their debts, and their estate was increased in value thereby to an amount in excess of the payments made. The account was a running account, and the effect of the payments was to keep it alive by the extension of new credits, with the net result of a gain to the estate of \$546.89, and a loss to the seller of that amount, less such dividends as the estate might pay. In these circumstances the payments were no more preferences than if the purchases had been for cash, and, as parts of one continuous bona fide transaction, the law does not demand the segregation of the purchases into independent items so as to create distinct pre-existing debts, thereby putting the seller in the same class as creditors already so situated, and impressing payments with the character of the acquisition of a greater percentage of a total indebtedness thus made up."

Peterson v. Nash, 7 A. B. R. 185, 112 Fed. 311 (C. C. A. Minn.): "Nash Brothers by delivering merchandise to the debtor, within four months next preceding the institution of proceedings in bankruptcy by her, and extending credit to her therefor and doing this in the ordinary course of business without knowledge of insolvency, in good faith enhanced the value of the debtor's estate, and while so doing, in like good faith, received payments on general account for an amount less in the aggregate than the value of the merchandise delivered to her. The giving and receiving under such circumstances, may properly enough be regarded as one transaction, resulting not in a preferential

⁸⁵. Compare discussion as to the right of offset, ante, § 1170, et seq. Compare [*Western*] *Tie & Timber Co. v. Brown*, 12 A. B. R. 111, 129 Fed. 728 (C. C. A. Ark., reversed 13 A. B. R. 447, 196 U. S. 502).

⁸⁶. Compare discussion as to "Net Results" under "Eighth Element of Preference," ante, § 1386; *Gans v. Ellison*, 8 A. B. R. 153, 114 Fed. 734 (C. C. A. Penn.); impliedly, *In re Sagor & Bros.*, 9 A. B. R. 361, 121 Fed. 658 (C.

A. N. Y.); *In re Topliff*, 8 A. B. R. 141, 114 Fed. 323 (D. C. Mass.); *In re Jourdan* (S. C. *Dickson v. Wyman*), 7 A. B. R. 186, 111 Fed. 726 (C. C. A. Mass.); *Carleton Dry Goods Co. v. Rogers*, 9 A. B. R. 787 (C. C. A. Tex.); *Morey Mercantile Co. v. Schiffer*, 7 A. B. R. 670, 114 Fed. 447 (C. C. A. Colo.). But see *In re Calton Export & Import Co.*, 8 A. B. R. 257 (affirmed in 10 A. B. R. 14, 121 Fed. 663, D. C. N. Y.).

payment to the creditor, but, in reality, in the creation of an indebtedness in favor of the creditor for the difference between the two."

§ 1419. Net Result, as to Enrichment of Estate after Insolvency, Test.—After the insolvency, the aggregate result to the trust fund, as to whether it has been enriched by the transaction taken as a whole notwithstanding the alleged preference, is to govern.

And the different items of payments, new goods, credits, etc., are not to be taken separately, nor are merely those new credits coming after any particular payment by the debtor to be offset against the payments preceding the particular new credits; but the transaction, after the insolvency within the four months, is to be taken as a whole and the net result taken.⁸⁷

In *re Geo. M. Hill Co.*, 12 A. B. R. 227, 130 Fed. 315 (C. C. A. Ills.): "We think that in stating the accounts between the parties, within the rule declared in *Jacquith v. Alden*, all the transactions between the parties must be included, and that we are not limited to an account as it is stated or was kept by the bank, because we are to inquire whether the net result of the transaction was to increase or decrease the estate of the bankrupt. If the account was stated including that amount, there remains no question that the net result of the dealings was to decrease the bankrupt's estate, and that the bank is therefore chargeable with the amount of that net decrease as a condition of proving its claim."

Yaple v. Dahl-Millikin Grocery Co., 11 A. B. R. 596, 193 U. S. 526: "Two questions are propounded by this certificate, namely:

"1. Where a creditor has a claim for a balance due against an insolvent debtor afterwards adjudged a bankrupt, upon an open account for goods sold and delivered four months before the adjudication in bankruptcy, and during said period makes a number of sales of merchandise on credit to the insolvent debtor, which becomes a part of the debtor's estate, and during the same period receives payments of sums on account, from time to time, which payments are received in good faith, without knowledge of the debtor's insolvency on the part of the creditor, the sales exceeding in amount during said period the payments made during the same time—has the creditor, under such circumstances, received a preference which he is obliged to surrender before his claim shall be allowed under the Bankrupt Act?

"2. If each of such payments is a preference under the act, is it to be set off, under § 60c of the Act, by deducting subsequent sales therefrom, carrying forward to the next payment any excess of preferences, but not of sales, treating any excess of preferences as thus ascertained as a sum to be surrendered before the allowance of the creditor's claim?"

⁸⁷. See ante, § 1296. *Jacquith v. Alden*, 9 A. B. R. 773, 189 U. S. 78, quoted at preceding paragraph. *Morrey Mercantile Co. v. Schiffer*, 7 A. B. R. 670, 114 Fed. 447 (C. C. A. Colo.); *Kimball v. Rosenham*, 7 A. B. R. 718, 114 Fed. 85 (C. C. A. Ark.); *Peterson v. Nash Bros.*, 7 A. B. R. 181, 112 Fed. 311 (C. C. A. Minn.); In *re Jourdan* (*S. C. Dickson v. Wyman*), 7 A. B. R. 186, 111 Fed. 726 (C. C. A. Mass.); In *re Watkinson*, 16 A. B. R. 38 (D. C. Penn.); In *re Delling*, 10 A. B. R. 688,

124 Fed. 852 (D. C. N. Y.); In *re King*, 7 A. B. R. 619, 113 Fed. 110 (D. C. Mass.); In *re Topliff*, 8 A. B. R. 141, 114 Fed. 323 (D. C. Mass.); contra, In *re Bailey*, 7 A. B. R. 26 (D. C. Vt.); contra, In *re Carlton Export & Import Co.*, 8 A. B. R. 257, affirmed in 10 A. B. R. 14, 121 Fed. 663 (D. C. N. Y.); compare, In *re Jones*, 10 A. B. R. 513 (D. C. S. C.). Compare, In *re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.).

"The first question is answered in the negative on the authority of *Jacquith v. Alden*, 189 U. S. 78, 9 Am. B. R. 773, and the second need not be answered."

Wild & Co. v. Provident Life & Trust Co., 22 A. B. R. 109, 214 U. S. 292, reversing 18 A. B. R. 506, 153 Fed. 562. "The facts of the case are simple. The bankrupt became insolvent on or before January 1, 1901, but the claimants had no knowledge of their insolvency during the running of the account hereafter referred to, and the merchandise therein specified was sold and delivered in the ordinary course of business. The appellants sold and delivered merchandise in various items, beginning February 14, 1901, and ending October 8, 1901. The total price of the merchandise thus delivered was \$3,377.28. There were payments on account on June 29 and October 10, amounting to \$811.36, leaving the net amount by which the bankrupt estate was enriched \$2,565.92. The last payment, on October 10, was \$634.78, and was two days after the last sale and delivery of merchandise. The single question in the case is whether that payment was a preference. It is conceded that it would not be a preference, in view of the other facts in the case, if it had been followed by a sale and delivery of goods of any value, however small. This concession is made necessary by the decision in *Jacquith v. Alden*, 189 U. S. 78, 9 Am. B. R. 733, * * * which is, in all respects, like the present case, except that two days after the payment which was alleged to be a preference, merchandise of trifling value was sold and delivered to the bankrupt. But the decision in that case was not rested upon the fact of this slight sale subsequent to the last payment. It was rather put upon the broader principle that all the dealings between the creditor and the bankrupt were after the bankrupt's insolvency, and that their net effect was to enrich the bankrupt's estate by the total sales, less the total payments. The majority of the court thought these facts distinguished the case from *Pirie v. Chicago Title & T. Co.*, 182 U. S. 438, 5 Am. B. R. 814, * * * though there was a difference of opinion upon that point. But all doubt was resolved in *Yaple v. Dahl-Millikan Grocery Co.*, 193 U. S. 526, 11 Am. B. R. 596, * * * where the precise question which is now here was decided by the court, and it was held, where a creditor has a claim upon an open account for goods sold and delivered during the period of four months before the adjudication in bankruptcy, the account being made up of debits and credits, leaving a net amount due from the bankrupt estate, that payments made under such circumstances did not constitute preferences which the creditor was bound to surrender before proving his claim in bankruptcy."

Compare, *In re Watkinson*, 17 A. B. R. 58 (D. C. Pa.): "We, therefore, hold that an increase of the bankrupt's estate, as a net result of the transactions between the bankrupt and a creditor within four months prior to filing the petition in bankruptcy where the last transaction was a payment on account of the indebtedness, is not sufficient to relieve the creditor from surrendering this last payment as preferential before he is permitted to prove the balance of his claim against the bankrupt's estate, when the account runs far back beyond the four months before the petition is presented and the transactions between them end with a large payment on account of the whole indebtedness. Under such circumstances it is a preferential claim and must be surrendered before the balance of the account of the creditor can be proven. *Kimball v. Rosenham Co.*, 7 Am. B. R. 718, 114 Fed. 85; *Sagor Bros.*, 9 Am. B. R. 361. Where in a running account payment by the bankrupt within the four months have induced new credits, which resulted in a net increase to the estate, the creditor may be said to have once surrendered his preference by the giving of the subsequent credit, but where, as in this case, the bankrupt, beginning far beyond the four months limit, makes a number of purchases, and then finally, within the four

months, makes a large payment on account, the creditor has been preferred. To hold otherwise would clearly give him a greater percentage of his debt than would be given to others of the same class."

§ 1420. Where Entire Transaction Occurs within Four Months and after Insolvency, No Preference.—Where the entire transaction—all the items of the running account—occur within the four months period and after insolvency, payments on account are not preferential and need not be surrendered.⁸⁸

§ 1421. Distinct Transactions with Same Creditor within Four Months, Not Severed.—Preference on one debt must be surrendered before any debt may be allowed. Distinct transactions with the same creditor within the four months period, provided of course they result in debts of the same "class," can not be severed. Thus, if the debtor owes the same creditor on a building contract; on a note for money borrowed and also on an open account for goods bought, all which obligations constitute debts of the same "class" within the purview of the bankruptcy act, and pays off in full two of these obligations under such circumstances as would render the payment preferences, the creditor can not have his claim on the third obligation allowed without surrendering the preferences on the other two. It makes no difference that the two transactions are "closed." All the transactions during the four months period and after insolvency, in the relation of debtor and creditor, are to be considered.⁸⁹

⁸⁸. *Jaquith v. Alden*, 9 A. B. R. 773, 189 U. S. 78 (affirming *Jaquith v. Alden*, 9 A. B. R. 165, C. C. A. Mass.); *Yaple v. Dahl Millakan Grocery Co.*, 11 A. B. R. 596, 193 U. S. 526; *In re Geo. M. Hill Co.*, 12 A. B. R. 221, 130 Fed. 315 (C. C. A. Ills.). Although in the *Yaple* and also in the *Hill Co.* cases the original account did not originate within the four months period as in the *Jaquith v. Alden*.

⁸⁹. *In re Rosenberg*, 7 A. B. R. 316 (Ref. N. Y.); *In re Jones*, 10 A. B. R. 513 (D. C. S. C.); contra, inferentially, *In re Lyon*, 10 A. B. R. 25, 121 Fed. 723 (C. C. A. N. Y., affirming 7 A. B. R. 412); contra, *The Abraham Steers Lumber Co.*, 7 A. B. R. 332, 112 Fed. 406 (C. C. A. N. Y.).

In cases involving "Innocent" preferences before the Amendment of 1903: *In re Conhaim*, 3 A. B. R. 249, 97 Fed. 924 (D. C. Wash.); *In re Beswick*, 7 A. B. R. 395 (Ref. Ohio); *In re Rogers Milling Co.*, 4 A. B. R. 540, 102 Fed. 687 (D. C. Ark.); *Dunn v. Gans*, 12 A. B. R. 316, 129 Fed. 750 (C. C. A. Penn.); *In re Bashline*, 6 A. B. R. 194, 109 Fed. 965 (D. C. Penn.); *Strobel v. Knost*, 99 Fed. 409; *Electric Corp'n v. Worden*, 3 A. B. R. 634, 99

Fed. 400 (C. C. A. Ind.); contra, *In re Abraham Steers Lumber Co.*, 7 A. B. R. 332, 112 Fed. 406 (C. C. A. N. Y.).

Contra, *In re Barrett*, 6 A. B. R. 199 (Ref. N. Y.): A case wrongly reasoned but right in its results since the payment of current rent is not the discharge of a pre-existing debt, but is the discharge of a contemporaneous obligation.

Contra, *Doyle v. Milw. Nat'l Bk.*, 8 A. B. R. 535, 116 Fed. 295 (C. C. A. Wis.); *In re Dickinson*, 7 A. B. R. 679 (Ref. N. Y.); *Wolf v. Levy*, 10 A. B. R. 153, 122 Fed. 127 (D. C. Tenn.); *In re Champion*, 7 A. B. R. 560 (Ref. Ala.); *In re Seay*, 7 A. B. R. 700, 113 Fed. 969 (D. C. Ga.).

Dividing of Indebtedness Ineffectual.—Much less can a creditor with an entire indebtedness avoid this result by dividing it by the taking of several distinct promissory notes therefor.

Dunn v. Gans, 12 A. B. R. 316, 129 Fed. 750 (C. C. A. Penn.): "We do not think that any fair construction of § 57 (g) would permit a creditor of an insolvent debtor to escape the penalty imposed by that section for receiving

Swarts v. Siegel, 8 A. B. R. 689, 117 Fed. 13 (C. C. A. Mo.): "A creditor who has received a preference on one claim against a bankrupt estate is thereby debarred from the allowance of any claim until the preference is first surrendered."

Livingston v. Heineman, 10 A. B. R. 39, 120 Fed. 786 (C. C. A. Ohio, reversing *In re New*, 8 A. B. R. 566): "Sometime within four months preceding the filing of the petition in bankruptcy the bank was the owner and legal holder of the two series of notes, which, in so far as the bank was concerned, and for the purposes of the administration of the bankrupt's estate, constituted but a single claim for \$9,000, no part of which could have been allowed, in favor of the bank, without the restoration to the bankrupt's estate of the two preferential payments. The disability of the bank in this respect inheres in the claim, and operates against the holder into whose hands it may come, whether by assignment or subrogation."

In re Teslow, 4 A. B. R. 757, 104 Fed. 229 (D. C. Minn.): "The prohibition (against proof of claim without surrender of preference) extends to all claims of such creditors against the estate of the bankrupt, and is not, as in the Act of 1867, confined to the claims 'on account of which the preference is made or given.'"

In re Meyer, 8 A. B. R. 598, 115 Fed. 997 (D. C. Tex.): "While the note for \$350 was given to settle a prior, separate, and distinct indebtedness on the part of the bankrupt to Walshe & Co., yet at the time of bankruptcy a portion of this note was still owing, and constituted a portion of the whole debt owing by the bankrupt to Walshe & Co. To rule that a creditor could withhold from proof a note upon which he had received substantial partial payments, and present for allowance other obligations of indebtedness without a surrender of partial payments received, would be, in the judgment of the court, to ignore the plain import of the language above quoted from the Bankruptcy Act."

In re Jourdan, 7 A. B. R. 186 (C. C. A. Mass.): "Section 57 (g) classifies according to creditors and not according to claims."

Swarts v. Fourth Nat'l Bk., 8 A. B. R. 673, 117 Fed. 1 (C. C. A. Mo.): "The unequivocal language and the unquestionable legal effect of this section are to prohibit the allowance of any claim of a creditor who has received a preference, either upon that or upon any other claim he holds against the estate of the bankrupt, unless he has first surrendered his preference."

In re Thompson's Sons, 10 A. B. R. 288, 289 (D. C. Penna., affirmed sub nom. *Gans v. Ellison*, 8 A. B. R. 153, 114 Fed. 734, C. C. A. Pa.): "It seems clear

a preference, by simply dividing the indebtedness into several amounts or parts, evidenced by several promissory notes. * * * We agree with the opinion of the court below that § 57 (g) of the Act of 1898 concerns creditors and not claims."

But where money was loaned to be used for a specific purpose but was not used at all, its return to the lender within the four months is not a preference. *Dressel v. North State Lumber Co.*, 9 A. B. R. 541, 119 Fed. 531 (D. C. N. Car.).

Creditor holding a claim for wages in excess of statutory amount, and extending back during all of the three months and for several months prior

thereto, can not apply payments received during the four months upon the items due before the three months and thus leave a priority claim for the full amount allowed by statute and a small common claim, but must surrender all the payments received by him within the four months as preferences—the payments cannot be considered as having been made on priority claims, for the claims were not priority claims when the bankruptcy actually occurred although they would have been priority claims had the bankruptcy occurred sufficiently earlier. *In re King Co.*, 7 A. B. R. 619, 113 Fed. 110 (D. C. Mass.).

that the purpose of the act was that among creditors proving their claims, one should not receive a greater proportionate share of the bankrupt estate than another. To make a distinction between a creditor who lends \$5,000 upon one promissory note and receives \$2,500 in part payment thereof, and another creditor who lends the same sum on two promissory notes and receives the same payment, is inequitable and unjust."

§ 1422. Subsequent Credit, to Extent of Security Given, Not to Be Offset.—The new credit must have been given without security of any kind, else it can not be offset, except as to the deficit in the value of the security.⁹⁰

§ 1423. Goods Purchased by Subsequent Credit Must Go to Enrich Estate.—The goods so purchased by the subsequent credit must go to form part of the estate.⁹¹

Bank of Wayne v. Gold, 26 A. B. R. 722 (App. Div. N. Y.), 130 N. Y. Supp. 942: "Counsel for appellant further urges that in any event it was entitled to recover certain advances made by it in connection with the mortgaged property after it had taken possession thereof under the mortgage, and before the bankruptcy proceedings were begun. This claim is made under subdivision 'c' of § 60 of the Bankruptcy Act. Reference to this provision of the act discloses that the further credit given the debtor by the creditor, which may be set off as therein provided, must not only be given in good faith and without security, but must also result in property which becomes a part of the debtor's estate. Whether any recovery for such alleged expenditure could in any event be had in the present action it is unnecessary now to determine; for the proof does not disclose that any part thereof resulted in any advantage to, or increase of, the mortgaged property."

Impliedly, *In re Morrow*, 13 A. B. R. 394, 134 Fed. 686 (D. C. Ohio): "Three years were given in which to pay the then existing indebtedness, and to keep the business going the bankrupts were to be supplied with goods from time to time, upon short credit, and, as the evidence shows, the goods so supplied were, in fact, used in carrying on the business."

But it need not be proved that the goods for which the unpaid new credit was given, remained part of the bankrupt estate up to the time of adjudication.

Kaufman v. Tredway, 12 A. B. R. 683, 196 U. S. 502: "The trial court, and its views were approved by the Superior Court, held that the statute required not merely that the creditor in good faith gave the debtor credit without security and that the money or property in fact passed to the debtor and became a part of his estate, but also that it remained such until the time of the bankruptcy and was transferred to the trustee, or at least that it was used in payment of preferred debts. * * *

⁹⁰. Bankr. Act, § 60 (c).

Inferentially, *In re Tanner*, 6 A. B. R. 196 (Ref. N. Y.): This was the case of a chattel mortgage being given to secure a floating balance of credit not to exceed a certain limited sum:

the credits given in excess of this sum held to be "without security of any kind."

⁹¹. Bankr. Act, § 60 (c). Impliedly, *Kaufman v. Tredway*, 12 A. B. R. 683, 196 U. S. 502.

"It will be noticed that the words used in paragraph 'c' are not 'the bankrupt's estate,' but 'the debtor's estate.' 'Debtor' is also found in the preceding clause as descriptive of the one to whom the credit is given. While the same person is both debtor and bankrupt, first debtor and then bankrupt, the use of the former term is suggestive of the time of the transaction as well as the status of the recipient of the credit. The paragraph further provides that 'the amount of such new credit remaining unpaid at the time of the adjudication in bankruptcy may be set off.' It is the nonpayment and not the fact that the property remains still a part of the debtor's estate which entitles to a set-off. It would seem that if Congress intended that which the trial court held to be of the meaning of the statute it would have said 'which becomes a part of the bankrupt's estate' or 'which becomes and remains a part of the debtor's estate until the adjudication in bankruptcy.' "

§ 1424. Creditor Must Have Acted in Good Faith in Acquiring Offset.—The creditor must have acted in good faith in the matter of acquiring the offset.⁹²

Kaufman v. Tredway, 12 A. B. R. 685, 196 U. S. 502: "Further, Congress provided that the creditor act in good faith. Thus it excluded any arrangement by which the creditor, seeking to escape the liability occasioned by the preference he has received, passes money or property over to the debtor with a view to its secretion until after the bankruptcy proceedings have terminated, or with some other wrongful purpose. It means that the creditor should not act in such a way as to intentionally defeat the Bankrupt Act, but should let the debtor have the money or property for some honest purpose. Requiring that it should become a part of the debtor's estate excluded cases in which the creditor delivered the property to a third person on the credit of the debtor, or delivered it to him with instructions to pass it on to some third party. The purpose was that the property which passed from the creditor should in fact become a part of the debtor's estate, and that the credit should be only for such property."

§ 1425. Payments upon Purchases on Subsequent Credit Not Themselves Preferences.—Any payments made upon the purchases thus made on the subsequent credit are not to be held preferences.⁹³

Impliedly, *In re Morrow*, 13 A. B. R. 394, 134 Fed. 686 (D. C. Ohio): "The payments were not intended to be applied upon the pre-existing indebtedness, the time for the payment of which had been extended one, two and three years, but were for goods which became a part of the bankrupt's estate."

§ 1425½. Offset Only Applicable upon Antecedent Preferential Transfers.—The offset is available only upon antecedent preferential transfers. The credit to be set off must be a "subsequent" credit. The credit may not be set off against a subsequent preferential transfer.⁹⁴

Price v. Derbyshire Coffee Co., 21 A. B. R. 280, 128 App. Div. 474, 112 N. Y. Supp. 830: "The complaint stated thirteen causes of action, each being pred-

⁹² Impliedly, *In re Morrow*, 13 A. B. R. 394, 134 Fed. 686 (D. C. Ohio).

⁹³ Compare same rule applied where payments were applied on the

old account, *In re Watkinson*, 16 A. B. R. 38 (D. C. Penn.).

⁹⁴ Also, *In re Beswick*, 7 A. B. R. 403 (Ref. Ohio). Also, see cases cited under § 1426.

icated upon the payment by the bankrupt of a promissory note made in favor of the defendant. These payments are alleged to have been made at various dates between January 2 and April 20, 1906. The set-offs claimed in the answer are for merchandise alleged to have been sold by defendant to the bankrupt upon credit on February 20 and March 9, 1906. We think that the fair and obvious construction of subdivision c of § 60 of the Bankruptcy Act is that further credits extended to a person who thereafter becomes a bankrupt, may be set off only against antecedent preferential payments, and not against such as may have been made after the extension of the new credits. It follows in the present case that the set-offs claimed by the defendants are inapplicable to some of the causes of action set forth in the complaint."

But of course such rule must be qualified so as not to include payments made, not on the pre-existing indebtedness, but upon the subsequent new credit.⁹⁵

§ 1426. "Innocently" Received Preferences before Amendment of 1903.—Before the Amendment of 1903 to the Bankruptcy Act it was held that preferences must be surrendered before the claim of the creditor could be "allowed," whether he had received the preference with reasonable cause to believe a preference was intended to be given him or not. In other words, preferences per se prevented, until surrender, the allowance of the preferred creditor's claim.⁹⁶

Flowing from these rulings quite a body of decisions grew up relative to so-called "innocently" received preferences, which, in many respects and upon many points, are still pertinent, although "innocently" received preferences need no longer be surrendered. Thus, as to the right of offset of new credits as well as other matters, the decisions as to "innocently" received preferences are in general still applicable and instructive.

§ 1427. "Surrender of Preferences" as Prerequisite to Allowance of Claim.—As to the requirement that preferences received by a creditor must be surrendered before his claim will be allowed, as also as to other matters of practice in the recovery of preferences, see ante, § 768, et seq.⁹⁷

⁹⁵. Compare, cases cited at § 1426; also, see § 1425.

⁹⁶. *Carson, Pirie v. Chic. Title & Trust Co.*, 5 A. B. R. 814, 182 U. S. 438.

⁹⁷. **Offsets to "Innocent Preferences" before Amendment of 1903.**—It was held, before the Amendment of 1903, that the same right of offset existed in relation to "innocently" received preferences as to those received with "reasonable cause for believing a preference was intended to be given." *McKey v. Lee*, 5 A. B. R. 267, 105 Fed. 923 (C. C. A. Ills.); *In re Ryan*, 5 A. B. R. 396, 105 Fed. 760 (D. C. Ills.); *In re Sechler*, 5 A. B. R. 579, 106 Fed. 484 (D. C. Kans.); *In re Christenson*, 4 A. B. R. 202, 101 Fed.

812 (D. C. Iowa); *In re Arndt*, 4 A. B. R. 773, 104 Fed. 234 (D. C. Wis.); *Morey Mercantile Co. v. Schiffer*, 7 A. B. R. 670, 114 Fed. 447 (C. C. A. Colo.); *Gans v. Ellison*, 8 A. B. R. 153, 114 Fed. 734 (C. C. A. Penn., affirming *In re E. O. Thompson's Sons*, 7 A. B. R. 214); *Kahn v. Export & Commission Co.*, 8 A. B. R. 157, 115 Fed. 290 (affirming *In re Southern Overall Mfg. Co.*, 6 A. B. R. 633, cited in *Dunn v. Gans*, 12 A. B. R. 316, C. C. A. Penn.); *In re Soldosky*, 7 A. B. R. 123, 111 Fed. 511 (D. C. Minn.); *In re Bothwell*, 8 A. B. R. 213 (D. C. N. J.); *Peterson v. Nash*, 7 A. B. R. 181, 112 Fed. 311 (C. C. A. Minn.); *In re Thompson's Sons*, 7 A. B. R. 214, 112 Fed. 651 (D. C. Penn., affirming 6 A.

§ 1428. **But Lien, Itself Not Preference, Not Denied Validity because Preference on Distinct Transaction Not Surrendered.**—But a lien which itself is not a preference is not to be denied validity because the lienholder has received a preference on a distinct transaction and has not surrendered the same. The prerequisite of surrender of preferences is applicable only when a claim is presented for allowance to share in dividends.⁹⁸ The trustee's remedy in other instances is a direct action to recover the preference.

SUBDIVISION "B."

LIENS BY LEGAL PROCEEDINGS NULLIFIED BY BANKRUPTCY.

§ 1429. **Second Branch of Trustee's Peculiar Title and Rights Conferred by Bankruptcy Act—Nullification of Liens by Legal Proceedings.**—We have now completed our study of the law relating to voidable preferences and of the circumstances which must exist in order to entitle the trustee in bankruptcy to recover the property affected by the preference for the benefit of the bankrupt estate; and in doing so we have finished one branch of the third and last division of the subject of the title and rights of the trustee. As will be recalled, the third division was taken up with the title conferred on the trustee by the peculiar provisions of the bankruptcy law itself in the protection of the insolvent fund from depletion: that is to say, from depletion by the debtor's voluntary act by way of voidable preferences; from depletion by the creditor's act irrespective of the debtor's co-operation, as by liens obtained by legal proceedings invalidated by bankruptcy; and from depletion by fraud, as by way of fraudulent conveyances within the four months preceding bankruptcy. We have finished with voidable preferences. We come now naturally to the second branch of the third division of the subject, and enter upon the consideration of the **invalidity of liens obtained by legal proceedings.**

All liens obtained by legal proceedings upon property of the bankrupt within four months preceding the filing of the bankruptcy petition and when he is insolvent, are nullified by the adjudication in bankruptcy.

Section 67 "f" of the Statute contains broad and sweeping, unequivocal and unescapable provisions annulling all liens, of every kind whatsoever, obtained by legal proceedings when the bankrupt was insolvent upon the

B. R. 663); *In re Beswick*, 7 A. B. R. 403 (Ref. Ohio); *In re Tanner*, 6 A. B. R. 196 (Ref. N. Y.); *In re Rosenberg*, 7 A. B. R. 316 (Ref. N. Y.); contra, *In re Abraham Steers Lumber Co.*, 7 A. B. R. 332, 112 Fed. 406 (C. C. A. N. Y., affirming 6 A. B. R. 315); contra, *In re Keller*, 6 A. B. R. 334, 109 Fed. 118 (D. C. Iowa); contra, *In re Oli-*

ver, 6 A. B. R. 626, 109 Fed. 784 (D. C. Iowa). Compare, *Wild & Co. v. Life & Trust Co.*, 18 A. B. R. 506, 153 Fed. 562 (C. C. A. Pa.), reversed, on other points, in 22 A. B. R. 109, 214 U. S. 292, quoted, on other points, at § 1419.
⁹⁸ *In re Franklin*, 18 A. B. R. 218, 151 Fed. 742 (D. C. N. Car.).

property of the bankrupt within the four months preceding the filing of the bankruptcy petition.⁹⁹

Clarke v. Larremore, 9 A. B. R. 476, 188 U. S. 486 (affirming *In re Kenney*, 5 A. B. R. 355, and 3 A. B. R. 353, and 2 A. B. R. 494): "The judgment in favor of petitioner was not like that in *Metcalf v. Barker*, one giving effect to a lien theretofore existing, but one which with the levy of an execution issued thereon created the lien; and as judgment, execution and levy were all within four months prior to the filing of the petition in bankruptcy, the lien created thereby became null and void on the adjudication of bankruptcy."

This section of the Bankruptcy Act was not repealed by the amendment of § 60b in the amendatory act of 1910.¹

§ 1430. Void, Irrespective of Constituting Acts of Bankruptcy.
—And such liens are void irrespective of their constituting acts of bank-

99. Bankr. Act, § 67 "f": "That all levies, judgments, attachments, or other liens, obtained through legal proceedings against a person who is insolvent, at any time within four months prior to the filing of a petition in bankruptcy against him, shall be deemed null and void in case he is adjudged bankrupt, and the property affected by the levy, judgment, attachment, or other lien shall be deemed wholly discharged and released from the same and shall pass to the trustee as a part of the estate of the bankrupt, unless the court shall, on due notice, order that the right under such levy, judgment, attachment, or other lien shall be preserved for the benefit of the estate, and thereupon the same may pass to and shall be preserved by the trustee for the benefit of the estate as aforesaid. And the court may order such conveyance as shall be necessary to carry the purposes of this section into effect: Provided, that nothing herein contained shall have the effect to destroy or impair the title obtained by such levy, judgment, attachment, or other lien, of a bona fide purchaser for value who shall have acquired the same without notice or reasonable cause for inquiry."

Metcalf v. Barker, 9 A. B. R. 43, 187 U. S. 165 (reversing *In re Lesser Bros.*, 5 A. B. R. 320); *In re Kemp*, 4 A. B. R. 242, 101 Fed. 689 (D. C. Colo.); *Bear v. Chase*, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S. C.); *In re Francis Valentine Co.*, 2 A. B. R. 522, 94 Fed. 793 (C. C. A. Calif., affirming 2 A. B. R. 188, 93 Fed. 935); *In re Richards*, 2 A. B. R. 518 (D. C. Wis., affirmed in 3 A. B. R. 145, 96 Fed. 937, C. C. A. Wis.); *In re Breslauer*, 10 A. B. R. 33, 121 Fed. 910 (D. C. N. Y.); *In re Kenney*, 3 A.

B. R. 353, 97 Fed. 557 (C. C. A. N. Y., affirmed in 5 A. B. R. 355, and affirming 2 A. B. R. 494, distinguishing 4 A. B. R. 220); *In re Reichman*, 1 A. B. R. 17, 91 Fed. 624 (D. C. Mo.); *In re Fellerath*, 2 A. B. R. 40, 95 Fed. 121 (D. C. Ohio); *In re Benedict*, 8 A. B. R. 463 (N. Y. Sup. Ct.); *In re Vaughn*, 3 A. B. R. 362, 97 Fed. 560 (D. C. N. Y.); *In re Higgins*, 3 A. B. R. 364, 97 Fed. 775 (D. C. Ky.); *In re Burrus*, 3 A. B. R. 296, 97 Fed. 926 (D. C. Va.); *Watschke v. Thompson*, 7 A. B. R. 504 (Sup. Ct. Minn.); *Maurau v. Carpet Lining Co.*, 6 A. B. R. 734 (Sup. Ct. R. I.); *In re Brown*, 91 Fed. 359; *In re Friedman*, 1 N. B. N. 208; *Mfg. Co. v. Mitchell*, 1 N. B. N. 262, 1 A. B. R. 701 (Ct. Com. Pleas Penn.); *Schmielovitz v. Bernstein*, 5 A. B. R. 264, 47 Atl. 884 (Sup. Ct. R. I.); *Lavor v. Seiter*, 5 A. B. R. 576 (N. Y. Sup. Ct., reversed, on other grounds, in 8 A. B. R. 459); *In re Kenney*, 2 A. B. R. 494, 95 Fed. 427 (D. C. N. Y., affirmed in 3 A. B. R. 353, 5 A. B. R. 355, 9 A. B. R. 476); *In re Richard*, 2 A. B. R. 506, 95 Fed. 258 (D. C. N. Car.); *Hardt v. Schuylkill Plush & Silk Co.*, 8 A. B. R. 479 (Sup. Ct. N. Y. App. Div.), obiter, *In re Weinger, Bergman & Co.*, 11 A. B. R. 427, 126 Fed. 875 (D. C. N. Y.); *In re Bailey*, 16 A. B. R. 289, 144 Fed. 214 (D. C. Ore.); *In re McCartney*, 6 A. B. R. 368, 109 Fed. 629 (D. C. Wis.); *In re Hammond*, 3 A. B. R. 490 (D. C. Mass.). Compare *Rome Planing Mill*, 3 A. B. R. 123, 96 Fed. 812 (D. C. N. Y.); *In re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa); *Cook v. Robinson*, 28 A. B. R. 182, 194 Fed. 753 (C. C. A. Alaska).

1. *In re Petersen*, 29 A. B. R. 26, 200 Fed. 739 (C. C. A. Ill.).

ruptcy.²

§ 1431. Void, Irrespective of Constituting Preferences.—And are void irrespective of their constituting preferences.³

Thus, they are void though the lien be not obtained upon a provable debt.⁴

§ 1432. Void, Irrespective of Consent or Permission of Debtor.—And are void irrespective of any consent or permission of the debtor.⁵

§ 1433. Void, Though Judgment Not Dischargeable.—And are void even though the judgment, upon which the levy was made or lien obtained, is not dischargeable.⁶

§ 1434. Void, Irrespective of Creditor's Knowledge of Debtor's Insolvency.—And are void irrespective of any knowledge by the creditor of the debtor's insolvency.⁷

§ 1435. Invalidating of Liens Obtained by Legal Proceedings Distinguished from Barring of Debt by Bankrupt's Discharge.—The invalidating of liens on the bankrupt's property by the adjudication in bankruptcy is to be distinguished from the barring of debts by the interposition of the bankrupt's discharge: the former concerns only proceedings in rem affecting assets, the latter only obligations in personam enforceable out of any new estate the bankrupt might obtain after adjudication.⁸

Bk. of Commerce v. Elliott, 6 A. B. R. 415, 85 N. W. (Wis.) 417: "Whether the court erred in refusing to give appellant judgment in form against Elliott obviously depends upon whether, after the discharge in bankruptcy and the entry of the plea by Elliott in bar of further prosecution of the main suit as to him, appellant had a cause of action in any sense upon which a judgment could be rendered. It is conceded that if a defendant is discharged in bankruptcy from a debt, pending proceedings to enforce it, he is entitled to plead such circumstances in bar of further proceedings for a personal judgment, if the plaintiff does not voluntarily discontinue the action, and to recover on such

2. In re Richards, 3 A. B. R. 145, 96 Fed. 935 (C. C. A. Wis., affirming 2 A. B. R. 518).

3. In re Richards, 3 A. B. R. 145, 96 Fed. 935 (C. C. A. Wis.); In re Baird, 11 A. B. R. 435, 126 Fed. 845 (D. C. Vt.); contra, In re Collins, 2 A. B. R. 1 (Ref. Iowa); contra, inferentially, In re Huffman, 1 A. B. R. 587 (Ref. Penn.); In re Peterson (Robinson v. Central Trust Co.), 29 A. B. R. 26, 200 Fed. 739 (C. C. A. Ills.).

4. Compare ante, § 1308, and post, § 1441½. Also, see In re Green, 24 A. B. R. 665, 179 Fed. 870 (D. C. Pa.), quoted post at § 1341½.

5. In re Richards, 3 A. B. R. 145, 96 Fed. 935 (C. C. A. Wis.).

6. In re Benedict, 8 A. B. R. 463 (N.

Y. Sup. Ct.); *Bear v. Chase*, 3 A. B. R. 746, 94 Fed. 793 (C. C. A. S. C.).

The rule that a stay will not be granted against a debt that is not dischargeable has reference to stays in behalf of the bankrupt to enable him to interpose his discharge and not to liens by legal proceedings within the four months, as to which stay will be granted though the debt be not dischargeable.

7. In re Richards, 3 A. B. R. 145, 97 Fed. 935 (C. C. A. Wis.).

8. See *Berry v. Jackson*, 8 A. B. R. 485 (Sup. Ct. Ga.). See post, § 2662, et seq., "Effect of Discharge on Rights of Parties." Instance, impliedly, *Sample v. Beasley*, 20 A. B. R. 164, 158 Fed. 606 (C. C. A. La.).

plea. But it is said that if an action is wholly in rem, or partly in rem and partly in personam, its status as an action to reach the res is not disturbed by a discharge of the defendant in bankruptcy, if the plaintiff's interest therein be preserved by the Bankruptcy Act. The authorities seem to be uniform to that effect."

Powers Dry Goods Co. v. Nelson, 7 A. B. R. 506, 10 N. Dak. 580: "The lien of an attachment on personal property of a bankrupt is not destroyed by a mere discharge of the debt secured by the lien, through a discharge under the present National Bankruptcy Act; and, unless such lien is one which is itself declared void by said act, it may be enforced, through a modified form of judgment, as against the property on which the lien exists."

§ 1436. Void, However, Only as to Trustee and Bankrupt, Not as to Lienholders.—The lien is not dissolved except for the benefit of the estate⁹ and of the bankrupt;^{9a} and if it is preserved for the benefit of the estate it is to be treated in determining priorities as still valid as to all other parties and lienholders interested in the property. But if not preserved, then it is annulled as to all lienholders as well as others.¹⁰

In explicating this clause "f" of § 67, the following propositions are to be borne in mind: There are five elements that must exist to make the lien void.

§ 1437. First Element Requisite to Nullify Lien by Legal Proceedings—Must Be Lien by Legal Proceedings.—The lien must have been obtained by legal proceedings and the legal proceedings must have created the lien.¹¹ Thus, liverymen's liens are not liens obtained by legal proceedings.¹² Thus, mechanics' liens do not come within these rules, for they are not liens created by legal proceedings, although the recording and filing of an affidavit or the institution of legal proceedings may be necessary to preserve or evidence them.¹³ Likewise, it was formerly queried whether a landlord's distraint was a legal proceeding;¹⁴

9. In re Merrow, 12 A. B. R. 615 (D. C. Mass.).

9a. Compare post, § 1447½; also *Chic., etc., R. Co. v. Hall*, 229 U. S. 511, 30 A. B. R. 619, wherein the Supreme Court holds that this provision redounds also to the benefit of the bankrupt.

10. *Thompson v. Failbanks*, 13 A. B. R. 437, 196 U. S. 516.

11. In re McKane, 18 A. B. R. 594, 152 Fed. 733, 155 Fed. 674 (D. C. N. Y.), quoted at § 1444. Compare, to same effect, In re Rome Planing Mills, 3 A. B. R. 123, 96 Fed. 812 (D. C. N. Y.).

In re Emslie, 4 A. B. R. 126, 102 Fed. 291 (C. C. A. N. Y.), where the District Court was reversed for holding a mechanic's lien void because the lien affidavit had been filed within the four months period, the Circuit Court of

Appeals holding this was not a lien obtained by legal proceedings.

In re Collins, 2 A. B. R. 1 (Ref. Iowa): This case is not authority, however, on all its other points. In re Drolesbaugh, 2 N. B. N. & R. 1029.

12. In re Pratesi, 11 A. B. R. 319, 126 Fed. 588 (D. C. Del.): A liveryman's lien is not dependent upon legal proceedings but is a perfect lien directly created by statute and as such is cognizable and enforceable in bankruptcy. In re Mero, 12 A. B. R. 171, 128 Fed. 630 (D. C. Conn.).

13. See ante, subdiv. "F," div. 2, "Trustee's Title as Successor to Bankrupt's Title," § 1155, et seq. Contra, (a poorly considered case, however), In re Monroe Lumber Co., 24 A. B. R. 371 (D. C. Miss.), quoted at § 1155.

14. In re Belknap, 12 A. B. R. 326, 129 Fed. 646 (D. C. Penn.).

some courts having held that it was a legal proceeding and that the lien thereof was invalidated by the bankruptcy,¹⁵ other courts having held that they are not legal proceedings creating the lien.¹⁶

It would seem that the Supreme Court of the United States has set the matter at rest, holding that landlord's distraint is not a lien by legal proceedings invalidated by § 67 of the Bankruptcy Act.

Henderson v. Mayer, 225 U. S. 631, 28 A. B. R. 389: "Similar rulings [see quotation of preceding portions of this decision at § 1155] have been made where the landlord has only a common-law right of distress. In *re West Side Paper Co.* (C. C. A. 3d Cir.), 20 A. B. R. 660, 162 Fed. 110, 89 C. C. A. 110. This is often referred to as a lien, but it is 'only in the nature of security.' 3 Black Com. 18. The pledge, or quasi-pledge, which the landlord is said to have, is, at most, only a power to seize chattels found on the rented premises. These he could take into possession and hold until the rent was paid. *Doe ex dem, Gladney v. Deavors*, 11 Ga. 84. But before the distraint the landlord at common law has 'no lien on any particular portion of the goods and is only an ordinary creditor except that he has the right of distress by reason of which he may place himself in a better position.' *Sutton v. Reese*, 9 Jur. (N. S.) 456.

"It is true that prior to levy it covers no specific property, and attaches only to what is seized under the distress warrant issued to enforce the lien given by statute. But in this respect it is the full equivalent of a common-law distress—the lien of which is held not to be discharged by 67f. * * * The fact that the warrant could be levied upon property which had never been on the rented premises does not change the nature of the landlord's right, though it may increase the extent of his security."

Similarly, in most States subcontractors' liens are held not to be liens created by legal proceedings; although in other States they are held to be created thereby.¹⁷

§ 1438. Liens from All Courts Equally Nullified.—Clause "f" applies to liens from any court, state or federal.¹⁸

§ 1439. All Kinds of Liens by Legal Proceedings Nullified.—Clause "f" applies to any kind of a lien by legal proceedings; thus, to a "Testatum fi. fa." issued within the four months;¹⁹ thus, to receiverships in equitable actions;²⁰ and, to receiverships in proceedings supplementary

15. In *re Dougherty Co.*, 6 A. B. R. 457, 109 Fed. 480 (D. C. Ga.).

16. In *re Seebold*, 5 A. B. R. 358, 105 Fed. 910 (C. C. A. La.); In *re West Side Paper Co.*, 20 A. B. R. 660, 162 Fed. 110 (C. C. A. Pa.), quoted at § 1160. See post, §§ 1444, 2204; In *re Robinson & Smith*, 18 A. B. R. 563, 154 Fed. 343 (C. C. A. Ills.), quoted at § 1444; *Plaut, trustee v. Gorham Mfg. Co.*, 23 A. B. R. 42, 174 Fed. 852 (D. C. N. Y.).

17. See ante, § 1156.

18. *Wood v. Carr*, 10 A. B. R. 577 (Ky. Court of App.).

19. *Mecke v. Rosenberg*, 9 A. B. R. 323, 202 Penn. St. 131.

20. In *re Brown*, 1 A. B. R. 107 (D. C. Ore.): In action to set aside a fraudulent conveyance. In *re Kersten*, 6 A. B. R. 516, 110 Fed. 929 (D. C. Wis.); *Hanson v. Stephens*, 11 A. B. R. 172, 42 S. E. 1028 (Sup. Ct. Ga.). So also, does clause "c" of § 67; *Coal Land v. Ruffner Bros.*, 21 A. B. R. 474, 165 Fed. 881 (C. C. A. W. Va.). Receivership in creditor's bill. *First Nat. Bk. v. Title & Trust Co.*, 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.), quoted and discussed at § 1603.

to executions;²¹ and, to receiverships over partnerships, dissolved by the death of a partner;²² and to receiverships to dissolve corporations;²³ likewise, to receiverships in foreclosure suits where property not covered by the lien is also sought to be sequestered;²⁴ also, to equity suits to reach the surplus of spendthrift trust income;²⁵ also to attachments;²⁶ and to attachments by mesne process where property has been sold but the proceeds are still in the officer's hands;²⁷ also to garnishment proceedings.²⁸

Klipstein v. Allen Miles Co., 14 A. B. R. 15, 136 Fed. 385 (C. C. A. Ga.): "Besides this the garnishment proceedings being had within four months prior to the bankruptcy proceedings, the surety is not relieved because of the discharge of the debtor because his bankruptcy avoided the lien acquired by the garnishment and destroyed the remedy by which a judgment could be recovered against the defendant which is indispensable to make the lien of any avail to the plaintiff."

And to creditors' bills.²⁹ And to receiverships under creditors' bills.³⁰

Dunn Salmon Co. v. Pillmore, 19 A. B. R. 172 (N. Y.): "Assuming that the commencement of the action by the plaintiff gave him a lien upon the claim against the defendant Pillmore, the lien was created within four months of the adjudication of bankruptcy, and when the defendant Jones was unquestionably insolvent, and hence was void under the Bankruptcy Act as against creditors. Section 67, subd. f. In other words, this particular creditor was prevented by the Bankruptcy Act from enforcing his rights as against the lien attempted to be created, because he would thereby gain a preference contrary to the Bankruptcy Act. * * * Although counsel have not argued the case upon that theory, it seems to me that the complaint may fairly be treated as the ordinary creditors' bill to set aside a transfer of the judgment debtor fraudulent against his creditors. In that view of the case, the lien created by the commencement of the action was void under the Bankruptcy Act; and, under the provisions of the Bankruptcy Act already referred to and under § 7 of article I of the Personal Property Law, being chapter 47 of the General Laws, the sole right to maintain an action for the benefit of the creditors resides in the trustee in bankruptcy."

21. *In re Tyler*, 5 A. B. R. 152, 104 Fed. 778 (D. C. N. Y.); *In re Matthews & Son*, 20 A. B. R. 570, 163 Fed. 127 (D. C. N. Y.).

22. *Wilson v. Parr*, 8 A. B. R. 230, 115 Ga. 629.

23. *Mauran v. Carpet Lining Co.*, 6 A. B. R. 734 (Sup. Ct. R. I.); *In re Lengert Wagon Co.*, 6 A. B. R. 535, 110 Fed. 927 (D. C. N. Y.).

24. *In re Knight*, 11 A. B. R. 1, 125 Fed. 35 (D. C. Ky.). Perhaps, *In re Hecox*, 21 A. B. R. 314, 164 Fed. 823 (C. C. A. Colo.).

25. *In re Tiffany*, 13 A. B. R. 310, 137 Fed. 314 (D. C. N. Y.).

26. *In re Brown*, 1 A. B. R. 107, 91 Fed. 358 (D. C. Ore.); *In re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa).

27. *Schmilovitz v. Bernstein*, 5 A. B. R. 265 (Sup. Ct. R. I.).

28. *In re McCartney*, 6 A. B. R. 368, 109 Fed. 629 (D. C. Wis.); *Hall v. Chicago, etc., Co.*, 25 A. B. R. 53 (Sup. Ct. Neb.); *In re Ransford*, 28 A. B. R. 78, 194 Fed. 658 (C. C. A. Mich.).

29. *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165 (reversing *In re Lesser Bros.*, 5 A. B. R. 320, C. C. A. N. Y.); *In re Adams*, 1 A. B. R. 94 (Ref. N. Y.); instance, *Continental Nat'l Bk. v. Katz*, 1 A. B. R. 19 (Superior Ct. Ills.); *First Nat. Bk. v. Title & Trust Co.*, 24 A. B. R. 330, 178 Fed. 187 (C. C. Pa.), quoted and discussed at § 1603.

30. *First Nat. Bk. v. Title & Trust Co.*, 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.), quoted and discussed at § 1603.

§ 1440. Including Lien Acquired by Creditors by General Assignments.—All kinds of liens by legal proceedings are thus nullified, including the lien acquired by creditors by virtue of statutes regulating assignments for the general benefit of creditors.³¹

§ 1441. Including Statutory Suits in Behalf of All Creditors for Setting Aside Fraudulent or Preferential Transfers Prohibited by State Law.—The better reason would seem to be that § 67 also includes the lien acquired by creditors by virtue of statutory suits for the setting aside of transfers fraudulent or preferential under State law and the administration and distribution of the debtor's property for the general benefit of all creditors.

Compare, *Miller v. Acid & Fertilizer Co.*, 21 A. B. R. 416, 211 U. S. 496: "It is obvious that if, at the time of the alleged preferential transfer to Miller, there were no other creditors of the individual estate of Guillory than Miller, under the rule laid down by the Bankrupt Act, the transfer to him of assets of the individual estate, in payment of an individual debt, did not constitute a preference. That it might have constituted a preference under the State law results from the difference in the classification made by the State law, on the one hand, and the bankruptcy law on the other. So, also, it is evident, having regard to the separation between the partnership and individual estates made by the Bankrupt Act and the method of distribution of those estates, that, if there were no individual creditors, and the sum paid to Miller was returned to the estate as a preference, it would be his right to at once receive back, by way of distribution, that which he was obliged to pay in upon the theory that it was a preference. * * * As the suit by the creditors was brought within four months before the adjudication in bankruptcy, their right to a lien or preference arising from the suit was annulled by the provisions of subdivision f of § 67 of the bankrupt law. But that section authorizes the trustee, with the authority of the court, upon due notice, to preserve liens arising from pending suits for the benefit of the bankrupt estate, and to prosecute the suits to the end for the accomplishment of that purpose."

One case, however, seems to make a distinction between suits brought to set aside transfers as fraudulent and suits brought not precisely to set aside transfers but rather to declare them, under the statute, to inure (as being preferential), to the benefit of all creditors joining in the suit, this case holding, in effect, that such a statutory suit regarding a transfer made be-

³¹ In re Fish Bros. Wagon Co., 21 A. B. R. 147, 164 Fed. 553 (C. C. A. Kans.), quoted at § 1489; inferentially, In re Andrae Co., 9 A. B. R. 135, 117 Fed. 561 (D. C. Wis.).

But compare, In re Gray, 3 A. B. R. 647 (N. Y. Sup. Ct. App. Div.): This case states an unnecessary rule—the assignment is void under § 67 (f) as creating a lien by legal proceedings, or under § 67 (c) as being created in fraud upon the Act. See post, "Superseeding of State Court's Custody in Cases of General Assignment," § 1602, et seq.

Chattel mortgage kept off record ten months, then filed, void by state law as against a trust mortgage for the benefit of certain creditors, thereafter executed, which trust mortgage itself is void as a preference by bankruptcy occurring within four months, held that the lien of the preference could not be preserved for the benefit of all creditors, to nullify the chattel mortgage, all occurring before the Amendment of 1910. *Rouse & Ottenwess v. Huxoll*, 31 A. B. R. 115, 208 Fed. 881 (C. C. A. Mich.).

fore the four months period, although instituted within the four months preceding bankruptcy, does not create a lien by legal proceedings within the purview of § 67 but simply "perfects," a "security," analogous to that of mechanics' liens; and that the bankruptcy court is to recognize the special rights of creditors so joining in the statutory suit and whether to grant them priority over other creditors under § 64 (b) (5), or permit them to go on with their statutory suit to its conclusion.

Moore v. Green, 16 A. B. R. 651, 145 Fed. 480 (C. C. A. W. Va., reversing *In re Porterfield*, 16 A. B. R. 11, 138 Fed. 192): "The proceeding in the State Court was one instituted under the statute of West Virginia, which enabled a creditor of an insolvent debtor to apply to a court of equity to vacate a preference in favor of a particular creditor, and have the conveyance declared to be for the benefit of all creditors properly joining in such suit. This suit was regularly instituted by the petitioner here, the holder of an unsecured debt of some \$3,700, and the same under said statute clearly inured to the benefit of himself and all other creditors authorized thereunder to intervene in the suit; and such rights could not, and should not, be destroyed by the subsequent act of the grantor in the trust deed in favor of his wife voluntarily waiting beyond the four months period, and then availing himself of the benefit of the Bankruptcy Act. Certainly such a result ought not to be brought about unless the interpretation of the bankruptcy law imperatively requires it. Until the husband chose to go into bankruptcy, his creditors had no right under the bankrupt law to require him so to do, he being a person 'engaged chiefly in farming or tillage of the soil,' and they had to look to the State law alone to ascertain their status respecting his property by assailing the deed made in favor of his wife, which they did. They could not anticipate that he would subsequently go into bankruptcy. Having thus availed themselves of the remedy prescribed by the State statute to enforce a right secured to them consequent upon the grantor's act while insolvent—to wit, the conveyances of his property to give a preference—upon instituting such proceedings in the State court they thereby became lienors and secured creditors, pursuant to said statute, under the deed of conveyance thus executed by the bankrupt, which conveyance the law declared upon the institution of the suit inured to the benefit alike of the secured creditor in the deed and his other creditors properly joining them. The true intent, spirit, and meaning of the Bankrupt Act, after enumerating the debts for which preference is thereby specially given, such as the payment of costs, taxes, etc., and certain labor claims, is to adopt the order of priority for the payment of debts prescribed by the State law; and by § 64b, subsec. 5, debts of the character here under consideration are plainly covered, namely, 'debts owing to any person who by the laws of the State is entitled to priority.' The debt secured by the trust deed of the 13th of June, 1902, to Mrs. Porterfield, the estate of whose husband is now being administered by the bankrupt court, would clearly be entitled to priority under the laws of West Virginia, under the deed securing the same, either in the State court or in the bankruptcy court sitting in said State. The debt itself has not been assailed, and the deed was apparently made in good faith, and within the time specified by the laws of the State under which the deed was given a proceeding was regularly taken, the effect of which was not to destroy the deed, but to cause the same, by reason of the insolvency of the grantor in the deed, to inure to the benefit of other creditors, as well as the beneficiary named in the deed. This was the condition existing at the time of the bankruptcy proceeding, and hence as to

the property covered by that deed to the extent of the debt therein secured the bankruptcy court took and possessed itself of such property impressed with the lien, and liable not alone to that of the beneficiary named in the deed, but subject to the rights of all persons whose interests had attached thereto by reason of the law of the State at the time of the institution of the bankruptcy proceeding. * * *

"The lien here claimed is analogous to that of mechanics, materialmen, sub-contractors, etc., which class of liens have been respected and enforced under the present Bankruptcy Act. They are given a lien by statute, but to be effective the same must be preserved and secured within a prescribed period by filing such claims, duly perfected, etc., for recordation in the designated court of the State. Being thus entitled to this inchoate lien, taking the steps to secure the benefit thereof within four months of bankruptcy has in every instance, so far as we are advised, been held not to be the taking of legal proceedings in contravention of the Act, but merely doing the necessary thing—taking the essential step—to secure the existing right under the statute. In this class of claims, by reason of the work done or supplies furnished under the agreement between the parties, the statute declares that there shall exist for the amount due a lien, upon the same being properly perfected. In this case the lien arises pursuant to the statute, and under and by virtue of the deed or transfer of the debtor's property, he being an insolvent, provided the creditors assail the same within the statutory period. To say that they should lose the right thus secured by taking the step necessary to secure or make the same effective would be an anomaly. This view of the law has been steadily maintained by the bankruptcy courts under the present Bankruptcy Act."

The effect of the holding in *Moore v. Green* was not especially wrong on the facts of the case, except perhaps for the refusal of the bankruptcy court to permit any other creditors to share in the property recovered than those who had joined in the statutory suit, but the reasoning seems full of dangerous doctrine.

By the same reasoning creditors' suits of all kinds, started within the four months period, would be valid wherever any transfer therein sought to be set aside was made before the four months period. They could all be held to be simply the "perfecting" of a "security" within the four months period, given before that period to the particular creditor invoking the statutory remedy.

The better reason would seem to be that § 67 also includes the lien acquired by creditors by virtue of statutory suits for the setting aside of transfers fraudulent and preferential under State law and the administration and distribution of the debtor's property for the general benefit of all creditors.

Compare, inferentially, and perhaps obiter, *First Nat. Bank v. Title & Trust Co.*, 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.): "Section 67f, like clauses 1, 2 and 3 of the first sentence of 67c, relates only to liens obtained for the benefit of less than all of the bankrupt's general creditors, and not to a lien which benefits all the creditors, and the dissolution of which will result in giving priority to particular creditors * * * As a lien acquired by a particular creditor may be preserved for the benefit of all creditors under § 67f, we see no reason why a lien acquired for the benefit of all creditors, especially where its

dissolution will result in giving priority to a particular creditor and thereby militate against the best interests of the general body of creditors, should not be preserved under 67c."

§ 1441½. Including Lien for Non-Provable or Non-Dischargeable Debt.—Liens by legal proceedings obtained on obligations that are themselves not provable or that are not dischargeable are equally as well nullified, for there is no qualification in the nullification of liens by legal proceedings corresponding to that of the avoidance of preferences, that the obligation on which the lien is obtained must be a provable debt. Thus, the levy of execution on a fine imposed by the State for the illegal selling of liquor has been held nullified.

In *re Green*, 24 A. B. R. 665, 179 Fed. 870 (D. C. Pa.): The grounds for the referee's decision seem to be that the claim of the commonwealth, being a fine, is not a provable claim in bankruptcy; that, not being provable, it will not be affected by a discharge of the bankrupt; and that, not being provable and not affected by the discharge of the bankrupt, the remedies provided by the State of Pennsylvania for the recovery of the judgment should not be affected by the Bankruptcy Act.

"It does not seem to us necessary to determine whether or not the judgment in favor of the commonwealth is provable, or whether or not the claim would be affected by the discharge of the bankrupt. It is sufficient to note that the commonwealth of Pennsylvania has recovered a lien upon the bankrupt's estate within four months prior to the filing of the petition in bankruptcy. I am satisfied that § 67f of the Bankruptcy Act makes no exceptions in favor of any lien creditor whose lien has been obtained through legal proceedings against the bankrupt within four months prior to the filing of the petition, other than such person who may have obtained title by virtue of such proceedings and has been a bona fide purchaser for value without notice or reasonable cause for inquiry."

§ 1442. "Legal Proceedings" Must Have Operated to Create Lien.—Legal proceedings must have operated to create the lien.³² Thus, replevin actions where title is claimed by the plaintiff are not within the prohibition of the section. The cause of action is inconsistent with a lien. It is the assertion of a right in the property itself as owner, not a claim of lien on another's property.

§ 1443. Unfounded Replevin Actions.—But where the replevin action is a mere excuse and without foundation, and is an attempt to seize assets of the bankrupt or to get a preference, it has been held that it will be void.³³

In *re Hymes Buggy & Implement Co.*, 12 A. B. R. 482, 130 Fed. 977 (D. C. Mo.): "The case at bar affords an apt illustration of the inequality and absurdity of allowing an exemption from the operation of § 67f in favor of a claimant who proceeds by writ of replevin. The evidence in this case shows that almost simultaneously with the institution of the replevin suit the petitioner

³² *Woods v. Klein*, 22 A. B. R. 722, 223 Pa. St. 257, quoted at § 1444. Also, compare all cases cited under § 1429, *et seq.*

³³ In *re Haynes*, 10 A. B. R. 715, 123 Fed. 1001 (D. C. Vt.). Compare facts, In *re Heinsfurter*, 3 A. B. R. 109, 97 Fed. 198 (D. C. Iowa).

instituted attachment proceedings against the bankrupt, indicating that it knew of the insolvency, and seized goods in the mass of property in said storehouse, but without segregating them. Becoming aware, doubtless, that the seizure under the writ of attachment would be nullified by the institution of proceedings in bankruptcy, the petitioner, under advice of counsel, let go, and resorted to the writ of replevin, the service of which was hardly complete when the proceedings in bankruptcy were instituted."

Obiter, In re Weinger, Bergman & Co., 11 A. B. R. 427, 126 Fed. 875 (D. C. N. Y.): "The strict meaning of the word 'levy' is usually a seizure of the defendant's property, but it does not seem to me a strained construction to hold, in view of the general purpose of this section, that it includes any seizure of property in the bankrupt's possession which he claims to own. If the language of § 67f is not comprehensive enough to cover a suit in replevin to recover property sold and delivered on credit, under a contract which the plaintiff claims a right to rescind for fraud, and a court of bankruptcy has no right to interfere for the protection of general creditors in this class of cases, very grave injustice may result."

But even in cases where the replevin action is thus a mere subterfuge, the proper practice would be for the trustee to intervene therein and assert his rights; for if it were a mere subterfuge, the replevin suit would fail and the trustee be thus vindicated. The plaintiff in the replevin suit is entitled to his day in court to prove it is not a mere subterfuge; and where else should he maintain his rights than in the suit itself?³⁴

§ 1444. Legal Proceedings Not Themselves Creating Liens but Merely Enforcing Pre-Existing Rights or Liens Not Affected.—Legal proceedings that do not themselves operate to create liens, but simply to enforce or give effect to pre-existing rights or liens, are not affected.³⁵

Obiter, *Clarke v. Larremore*, 9 A. B. R. 478, 188 U. S. 486: "The judgment was not, like that in *Metcalf v. Barker*, one giving effect to a lien theretofore existing, but one which with the levy of execution thereon created the lien."

Thus, § 67f does not refer to seizures by replevin.³⁶ Likewise, foreclosure suits, where no new lien is created but merely a former valid lien enforced, are not affected.³⁷

³⁴. Impliedly, In re Rudnick & Co., 20 A. B. R. 33, 160 Fed. 903 (C. C. A. N. Y.), quoted at § 1585.

³⁵. See post, "Conflict of Jurisdiction," § 1586. *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165 (reversing In re Lesser Bros., 5 A. B. R. 320, C. C. A. N. Y.); In re Kavanaugh, 3 A. B. R. 832, 99 Fed. 928 (D. C. Ky.); contra, In re Knight, 11 A. B. R. 1, 125 Fed. 35 (D. C. Ky.): But in this case the receivership operated to do more than enforce existing valid liens. Also, see ante, §§ 1160, 1437; post, §§ 1501, 1589, 224. In re Matthews & Son, 20 A. B. R. 570, 163 Fed. 127 (D. C. N. Y.); In re McKane, 18 A. B. R. 594, 152 Fed. 733, 155 Fed. 674 (D. C.

N. Y.); *Colston v. Austin, etc., Co.*, 28 A. B. R. 92, 194 Fed. 929 (C. C. A. Del.), quoted at § 1384½; In re Van Da Grift, etc., Co., 27 A. B. R. 474, 192 Fed. 1015 (D. C. Ky.).

Contra, In re Monroe Lumber Co. (a poorly considered case, however), 24 A. B. R. 371 (D. C. Miss.), quoted at § 1155.

³⁶. See ante, § 1443; post, § 1585.

³⁷. See post, "Conflict of Jurisdiction," § 1586.

Instance (though also instituted before the four months—an immaterial consideration), *Sample v. Beasley*, 20 A. B. R. 164, 158 Fed. 606 (C. C. A. La.).

Woods v. Klein, 22 A. B. R. 722, 223 Penn. St. 257: "The appellee acquired no right or lien as a preference over other creditors of the appellant within four months of the institution of the bankruptcy proceedings. What he did within that period was the exercise of a right and the enforcement of a lien which had been acquired 18 months before. The right was to take possession of the mortgaged boat and sell it at any time upon the default of the mortgagor. The preference was obtained when the lien attached in 1905, and not when it was enforced in 1907. No provision of the Bankrupt Act contemplates that a valid lien, acquired more than four months before the filing of a petition in bankruptcy shall be vacated by the bankruptcy proceedings, or that the enforcement of such a lien by execution shall constitute an illegal preference. *Owen v. Brown*, 9 Am. B. R. 717, 120 Fed. 812 (C. C. A.). There is a clear distinction between the bald creation of a lien within the four months and the enforcement of one previously acquired. * * * The lien that is invalidated by the Bankrupt Act is one created by a levy, judgment, attachment, or otherwise, within four months. Where the lien is obtained more than four months prior to the institution of the bankruptcy proceedings, it is not only not to be deemed null and void on an adjudication of bankruptcy, but its validity is recognized. When the lien is obtained within four months, the property of the bankrupt is discharged therefrom, but not otherwise."

In *re McKane*, 18 A. B. R. 594, 152 Fed. 733, 155 Fed. 674 (D. C. N. Y.): "As to the second motion, in which a stay of the sale under the foreclosure is asked, a hasty examination seems to indicate, from the reasoning set forth in the case of *Metcalf v. Barker*, 187 U. S. 165, 9 Am. B. R. 36, that the judgment in foreclosure has not created the lien, and is not within the provisions of § 67f. The judgment is merely a decree by a court having competent jurisdiction directing the enforcement of a lien which can not be affected or vacated by bankruptcy proceedings."

Nor are seizures by the sheriff on execution of property already mortgaged to the same creditor for the same debt affected; ³⁸ nor does § 67 "f" refer to proceedings to give effect to landlord's liens.

In *re Robinson & Smith*, 18 A. B. R. 563, 154 Fed. 343 (C. C. A. Ills.): "And the claim of appellant is that the seizure in distress is, within these paragraphs, in the nature of a suit or proceeding in attachment, and having been begun within the four months before bankruptcy, is annulled by the adjudication of bankruptcy. We can not concur in this view. The whole question is one of interpretation of the Bankruptcy Act—the policy of that act respecting the recognition of liens in the distribution of bankrupt estates. Paragraphs 'c' and 'f' quoted were meant, in our judgment, to relate only to those actions or proceedings taken by creditors, who having no existing lien or right of lien resting in existing contract, entered into in good faith, seek to obtain preference by being first in a race of diligence—a preference that the bankruptcy law annuls, because the purpose of that law is to substitute equality for diligence. But the lien obtained by the distress warrant under the kind of lease involved in this case is not the result of a race of diligence. Under the lease, and the Illinois law interpreting the lease and the rights of the parties thereunder (*Powell v. Dailey*, 163 Ill. 646, 45 N. E. 414; *Atkins v. Byrnes*, 71 Ill. 332) the right of lien was created when the lease was executed, and the tenant entered upon possession of the premises—a right put wholly, at that time, within the control of the landlord, and maturing the mo-

38. Analogously, In *re Chapman*, 3 A. B. R. 607, 99 Fed. 395 (D. C. Ga.); contra, In *re Booth*, 2 A. B. R. 770, 96 Fed. 943 (D. C. Ga.).

ment the landlord chose to mature it. And though it did not actually attach (as in the New York case, 4 Am. B. R. 126, 102 Fed. 292, *supra*) until within four months of the bankruptcy, it was the kind of lien, it seems to us, that § 67d was intended to preserve; for unquestionably as between the parties to the lease it was a lien, not simply because the distress warrant was actually levied, but because, by contract between them, the levy of the distress warrant was authorized; and as against creditors, such a lien prevails from the moment it is made a matter of record or public notice, not solely because by such record or notice the lien attaches, but because, from the moment of such record or notice, the creditors are informed that the lien, or the right to such lien, had been in existence from the time that the contract authorizing it was entered into. In other words, the lien is not one that the creditor has obtained irrespective of any right or lien given him by the debtor, but wholly by resort to the judicial proceedings in law or equity that are open to all; but is a lien given directly by the debtor and accepted by the creditor, in good faith, and not in contemplation of bankruptcy—just the kind of relationship that distinguishes a lien attaching as the result of contract, from a lien springing out of some independent and adverse proceedings.”

Nor will it cause the bankruptcy court to supersede the custody of the State court under levy thereon.³⁹

Nor does it refer to warrants of eviction in landlord's proceedings to recover possession of leased premises.⁴⁰

Nor does it refer to the mere appointment, within the four months, of a receiver in supplementary proceedings, where the supplementary proceedings were instituted before the four months, property not being seized by him.⁴¹

§ 1445. Lien Valid in Part, and Void as to Balance.—Where the suit is in part a mere foreclosure suit or other suit to realize upon a valid pre-existing lien, and in part creates a lien by legal proceedings upon other assets of the insolvent during the four months period, the legal proceedings will be valid as to the first part and be nullified as to the latter, and the custody of the State Court will be preserved as to the first part and be superseded as to the latter part.⁴²

§ 1446. Receiverships, etc., May Operate to Create “Liens by Legal Proceedings.”—And mere receiverships, even before the Amendment of 1903 made them acts of bankruptcy, were held to be legal liens and to be supplanted by subsequent bankruptcy proceedings.⁴³

39. In re Seebold, 5 A. B. R. 358, 105 Fed. 910 (C. C. A. La.); In re West Side Paper Co., 20 A. B. R. 660, 162 Fed. 110 (C. C. A. Pa.), quoted at § 1160.

40. Plaut, trustee, v. Gorham Mfg. Co., 23 A. B. R. 42, 174 Fed. 852 (D. C. N. Y.). Compare, as to forum, however, post, §§ 1796, 1799.

41. Wrede v. Clark, 21 A. B. R. 821 (N. Y. Sup. Ct. App. Div.), quoted at § 1455.

42. Carling v. Seymour Lumber Co.,

8 A. B. R. 30, 113 Fed. 483 (C. C. A. Ga.). But compare, *Coal Land Co. v. Ruffner Bros.*, 21 A. B. R. 474, 165 Fed. 881 (C. C. A. W. Va.), quoted at §§ 1603, 1902.

43. *First Nat. Bk. v. Title & Trust Co.*, 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.), quoted post at § 1603; *Wilson v. Parr*, 8 A. B. R. 234, 115 Ga. 629; *Moore v. Green*, 16 A. B. R. 651, 145 Fed. 480 (C. C. A. W. Va.). See subject of “Assignment and Receiverships,” post, § 1603.

Mauran v. Carpet Lining Co., 6 A. B. R. 739 (Sup. Ct. R. I.): "It seems to us that the word 'judgment,' as used above, is sufficiently broad to apply to the judgment of this court in appointing the receiver of the Crown Carpet Lining Co., and that the adjudication of bankruptcy against said corporation nullified and avoided the judgment of this court, and that the property held by the receiver must be turned over for administration under the bankruptcy proceedings. * * *

"For the reasons above stated, we are of the opinion that the application of the trustee in bankruptcy that the funds in the hands of the receiver appointed by this court be turned over to him, must be granted."

And in some cases are held to be supplanted by virtue of § 67c instead of by § 67f.⁴⁴

§ 1447. Second Element Requisite to Nullify Liens by Legal Proceedings.—The lien must have been obtained upon property which otherwise would have gone into the bankrupt's estate to swell the trust fund for all creditors, or upon exempt property, or upon property affected by some transfer or lien which itself in turn is void under state law as to the lien by legal proceedings concerned or inferior in priority thereto.⁴⁵

Where a writ of attachment has been levied within the four months period and while the bankrupt was insolvent, but has been discharged by an undertaking for which the surety takes no security from the bankrupt's estate, the writ will not be vacated after the adjudication in bankruptcy so as to discharge the surety, for the bond has taken the place of the bankrupt's property.^{45a}

44. *Coal Land Co. v. Ruffner*, 21 A. B. R. 474, 165 Fed. 881 (C. C. A. W. Va.); *First Nat. Bk. v. Title & Trust Co.*, 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.), quoted at § 1603.

45. Impliedly, perhaps, *In re Durham*, 4 A. B. R. 760, 104 Fed. 231 (D. C. Ark.), which was a case of a sheriff's seizure of exempt property after adjudication where there were no exemptions against purchase price levy. *Jewett Bros. v. Huffman*, 13 A. B. R. 738 (N. Dak.); *McKinney v. Cheney*, 11 A. B. R. 54, 118 Ga. 387; obiter *Powers Dry Goods Co. v. Nelson*, 7 A. B. R. 506 (Sup. Ct. N. Dak.).

Impliedly (perhaps), *White v. Thompson*, 9 A. B. R. 653, 119 Fed. 868 (C. C. A. Ala.), which was a case of attachment of exempt property, although the decision was placed on other grounds. Impliedly, *In re Allen & Co.*, 13 A. B. R. 518, 134 Fed. 620 (D. C. Va.); obiter, *In re Hopkins* 1 A. B. R. 209 (Ref. Ala.). But see contra, *In re Tune*, 8 A. B. R. 285, 115 Fed. 906 (D. C. Ala.). Inferentially, contra, *In re Bolinger*, 6 A. B. R. 171, 108 Fed. 374 (D. C. Penn.), in which, how-

ever, the levy was held void, as creating a "preference," Impliedly, contra, *In re Beals*, 8 A. B. R. 639, 116 Fed. 530 (D. C. Ind.). Contra, *In re McCartney*, 6 A. B. R. 366, 109 Fed. 621 (D. C. Wis.).

Compare, inferentially, *In re Lehigh Lumber Co.*, 4 A. B. R. 221 (D. C. Penn.), where the court impliedly holds that a lien obtained within four months of a partnership bankruptcy, upon the individual property of a non-bankrupt member, is not void, although of course it must be conceded the individual assets are sub modo a fund for the firm creditors. See ante, "Exemptions," § 1100.

Inferentially, *In re Shinn*, 25 A. B. R. 833, 185 Fed. 990 (D. C. N. J.).

Instance, *American Steel & Wire Co. v. Coover*, 25 A. B. R. 58 (Sup. Ct. Okla.), which was a case of an attachment of partnership property which was not nullified because of the adjudication of a member of the firm.

45a. *Nat'l Surety Co. v. Medlock*, 19 A. B. R. 654, 2 Ga. App. 665, 58 S. E. 1131, quoted at § 1455.

King v. Block Amusement Co., 20 A. B. R. 784, 126 App. Div. 48, 111 N. Y. Supp. 102: "Counsel for appellant contends that the effect of these provisions is merely to discharge the lien of the attachment, and not to vacate the writ. He concedes that, so far as the bankrupt is concerned, the cause of action has been discharged, but he urges that his client should be permitted to proceed to judgment against the bankrupt with a perpetual stay against the enforcement of the judgment against the bankrupt, which would protect the latter in all the rights guaranteed by the Bankruptcy Act, and at the same time would enable the plaintiff to enforce the liability of the surety on the undertaking. Authority for that course is found in many cases where the warrant of attachment was procured more than four months prior to the filing of the petition in bankruptcy. *Hill v. Harding*, 130 U. S. 699; *Holyoke v. Adams*, 59 N. Y. 233; *Metcalf v. Barker*, 187 U. S. 165, 9 Am. B. R. 36. See, also, *Hillyer v. Le Roy*, 12 Am. B. R. 733, 179 N. Y. 369, and *Pikert v. Eaton*, 81 App. Div. 423. In all of these cases it is to be borne in mind that unless the right of the plaintiff to continue the action to judgment were preserved he would lose the lien duly acquired by the attachment or the benefit of the security of the undertaking which took its place. The effect of the contention of the learned counsel for appellant would be to place his client in a better position by having obtained the undertaking, than if the levy had stood upon the property, for it is clear that under the provisions of the Federal statute herein quoted, if no undertaking had been given to discharge the levy, the levy would be discharged by the decree in bankruptcy and the trustee in bankruptcy would be entitled to the property. In that event the plaintiff's only right would have been to share with other general creditors in his proportion of the proceeds derived from the sale of the property. It is conceded that if the surety had taken security, it would be the duty of the court under subdivision f of § 67 of the Bankruptcy Act to vacate the warrant of attachment as a condition of requiring the surety to deliver over to the trustee in bankruptcy the property pledged. It is argued in behalf of respondent that since the attachment was issued within four months of filing the petition in bankruptcy, and the lien thereof, if the undertaking had not been given, would have been discharged by the bankruptcy of the defendant, the plaintiff has not been prejudiced by the giving of the undertaking, and a construction should not be placed upon the act which would give the plaintiff the advantage of holding the surety on the undertaking when he could not have held the property under the attachment and that the proper construction of these provisions of the Bankruptcy Act is that where the lien is acquired by virtue of a judgment or warrant of attachment recovered or issued within four months of filing the petition in bankruptcy both the lien and the instrument under which it was acquired should be deemed null and void, * * * and the United States Circuit Court of Appeals, Fifth Circuit, so held, in effect, in *Klipstein & Co. v. Allen-Miles Co.*, 14 Am. B. R. 15, 136 Fed. 385. Our Court of Appeals, however, held under the Bankruptcy Act of 1867, which, although different in terms on this point, is not sufficiently different in substance to warrant us in distinguishing and not following the authority, that a warrant of attachment which had been issued within four months of filing the petition in bankruptcy and had been discharged by a similar undertaking but not vacated, was unaffected, at least as to the surety, by the subsequent adjudication in bankruptcy and discharge of the bankrupt, and that where the action was prosecuted to judgment the liability of the surety became thereby fixed. *McCombs v. Allen*, 82 N. Y. 114. In the case at bar this court following *Holyoke v. Adams*, supra, recently held that this defendant should not be permitted to amend its answer by setting up its discharge in bankruptcy which would prevent plaintiff obtaining judgment upon

which the liability of the surety might be enforced. 125 App. Div. 922. It would seem to follow that the defendant was not entitled to have the warrant of attachment vacated. We are not concerned with the question as to the remedy of the surety over against the estate in bankruptcy or against the bankrupt personally in the event that it shall be obliged to pay any judgment that may be recovered herein (see *Hill v. Harding*, supra, and *Klipstein & Co. v. Allen-Miles Co.*, supra), and no opinion is expressed on those points."

But after such lien by legal proceedings has been acquired, subsequent transfers may have been made or liens may have been acquired that would have prevented the property passing to the trustee even if the lien by legal proceedings were extinguished. In such event the lien is void only in a certain way, namely, it is void as to the trustee but is good as to subsequent transferees and lienholders, and if it is preserved for the benefit of the bankrupt estate, the trustee gets the advantage of the priority of the lien by legal proceedings, but uses such advantage for the benefit of all creditors.

First National Bk. v. Staake, 15 A. B. R. 644, 202 U. S. 141: "The argument is based upon the theory that the second clause was not intended to apply to liens acquired upon the estate of third parties, but to property which would have passed to Baird's trustee had the attachment not been levied. In other words, that the bankruptcy court has nothing to do with the property, since it really did not belong to the bankrupt, and would have passed to his vendee if the attachments had not been levied upon it. Indeed the opinion especially finds that 'had valid attachments not been levied, the property would have passed to the trustee of the Roanoke Furnace Company.'

"To what extent liens obtained by prior judicial proceedings shall be recognized is a matter wholly within the discretion of Congress. It might have validated all such liens, even though obtained the day before proceedings were instituted. It might probably have invalidated all such liens whenever obtained. It took a middle course, and invalidated all liens obtained through legal proceedings within four months prior to the filing of the petition, but at the same time preserved to the general body of creditors, as against third parties (such as purchasers under an unrecorded deed), such liens as attaching creditors had secured upon property which would have passed to the subsequent purchaser in case the attachment had not been levied. It is true that the attaching creditors are thereby deprived of the fruits of their diligence, but the same thing would have happened had the attachment been levied upon property to which the bankrupt had the whole and undisputed title, or of which he had made a fraudulent conveyance. As remarked by the District Judge, 'In cases where the bankrupt makes a valid conveyance, or where his fraudulent vendee makes a valid conveyance, the purpose of the law is worked out by preserving and enforcing the liens of the attaching creditors for the pro rata benefit of all the creditors.'

"Section 67f is merely carrying out the general purpose of the Act, of securing to the creditors the entire property of the bankrupt, reckoning as part of such property liens obtained by attaching creditors against real estate which had been transferred to another, though no deed had been actually executed and recorded.

"The argument that § 67f in question here, refers only to liens upon property which, if such liens were annulled, would pass to the trustee of the bankrupt, we think is unsound, since that contingency is amply provided for by the prior clause of the section annulling all such liens, and providing that property af-

affected thereby shall pass to the trustee as a part of the estate. Under the argument of the attaching creditors in this case, the subsequent clause would be entirely unnecessary. This clause evidently contemplates that attaching creditors may acquire liens upon property which would not pass to the bankrupt, if the liens were absolutely annulled, and therefore recognizes such liens, but extends their operation to the general creditors. Had no proceedings in bankruptcy been taken doubtless this property would have been sold for the benefit of the attaching creditors."

Property affected by a transfer or lien which itself is void as to the nullified "lien by legal proceedings within four months" will pass to the trustee even though it would not have passed to the trustee if the nullified lien never had existed. In other words the nullified lien may be used as an instrument to avoid other liens or transfers which themselves would not be avoided by the bankruptcy.

Martin v. Globe Bank & Trust Co., 27 A. B. R. 553, 193 Fed. 841 (C. C. A. Ky.): "It is insisted, however, that these decisions are not relevant, because under § 1907 of the Statutes of Kentucky the deed was valid, except as to those creditors whose debts were existing at the date of its delivery; and that, since the banks were the only creditors of that class who obtained liens through the commencement of suits and levies of attachments, the benefits of such liens cannot be extended to anyone else. * * * As respects liens so acquired within the four months, it is difficult to conceive of language of wider scope than this [67c and 67f]. It is not claimed that Atkins was not insolvent at the time these suits were commenced and the attachments levied, and the reason for this is obvious. Atkins was adjudicated a bankrupt within the next succeeding four months, and the present controversy leaves no room for doubt as to his insolvency at the date of the suits and attachments. If the distinction urged on behalf of the banks were sound, it is hard to perceive why it would not be applicable to every case where some of a body of creditors, who all admittedly have equal rights, are more diligent than the others in securing liens through attachments or any of the other means stated in 67c and f; for all the practical results and hardships among the creditors would in that event be identical with those complained of here. It is plainly within the power of Congress to enact that liens so acquired within a specified period should, through bankruptcy proceedings, be applied to the common benefit of all the creditors of a bankrupt."

§ 1447½. **Exempt Property.**—It was for a long time a disputed question whether liens by legal proceedings obtained within the four months period upon exempt property were nullified by the bankruptcy,⁴⁶ but the question has been definitely set at rest by the Supreme Court of the United States to the effect that liens by legal proceedings on exempt property are nullified equally with those on non-exempt property.

Chicago, etc., R. Co. v. Hall, 229 U. S. 511, 30 A. B. R. 619 "* * * he insists that if there was a lien against his wages, it was obtained by garnishment served within four months of his bankruptcy and discharged by virtue of the provisions of § 67f. * * * The railroad, on the other hand contends that under § 70 the trustee acquires no title to 'property which is exempt' and that

46. See ante, § 1100.

liens thereon are not discharged by § 67f, since that section has reference only to liens on property which can 'pass to the trustee as part of the estate of the bankrupt.' On this question there is a difference of opinion, some state and federal courts holding that the Bankruptcy Act was intended to protect the creditors' trust fund and not the bankrupt's own property and that therefore liens against the exempt property were not annulled even though obtained by legal proceedings within four months of the filing of the petition. In *re Driggs* (D. C. N. Y.), 22 A. B. R. 621, 171 Fed. 897; *Re Durham* (D. C. Ark.), 4 A. B. R. 760, 104 Fed. 231. On the other hand, *Re Tune* (D. C. Ala.), 8 A. B. R. 285, 115 Fed. 906; *Re Forbes* (C. C. A. 9th Cir.), 26 A. B. R. 355, 186 Fed. 79, hold that 67f, annuls all such liens, both against the property which the trustee takes and that which may be set aside to the bankrupt as exempt. This view, we think, is supported both by the language and the general policy of the Act which was intended not only to secure equality among creditors, but for the benefit of the debtor in discharging him from his liability and enabling him to start afresh with the property set apart to him as exempt. Both of these objects would be defeated if judgments like this present were not annulled, for otherwise the two Iowa plaintiffs would not only obtain a preference over other creditors, but would take property which it was the purpose of the Bankruptcy Act to secure to the debtor.

"Barring exceptional cases, which are specially provided for, the policy of the Act is to fix a four months period in which a creditor cannot obtain an advantage over other creditors nor a lien against the debtor's property. 'All liens obtained by legal proceedings' within that period are declared to be null and void. That universal language is not restricted by the later provision that the property affected by the * * * lien shall be released from the same and pass to the trustee as a part of the estate of the bankrupt. It is true that title to exempt property does not vest in the trustee and cannot be administered by him for the benefit of creditors. But it can pass to the trustee as a part of the estate of the bankrupt for the purposes named elsewhere in the statute, included in which is the duty to segregate, identify and appraise what is claimed to be exempt. * * * In other words, the property is not automatically exempt, but must 'pass to the trustee as a part of the estate'—not to be administered for the benefit of creditors, but to enable him to perform the duties incident to setting apart to the bankrupt what, after a hearing, may be found to be exempt. Custody and possession may be necessary to carry out these duties and all levies, seizures and liens obtained by legal proceedings within the four months that may or do interfere with that possession are annulled. * * * The section does not, however, defeat rights in the exempt property acquired by contract or by waiver of the exemption. These may be enforced or foreclosed by judgment obtained even after the petition in bankruptcy was filed under the principle declared in *Lockwood v. Exchange Bank*, 190 U. S. 294, 10 A. B. R. 107, 47 L. Ed. 1061, 23 Sup. Ct. Rep. 751. * * * Those liens having been annulled by § 67f of the Bankruptcy Act, furnished no defense for the railroad when sued by Hall for his wages, earned in Nebraska, exempt by the laws of that state and duly set apart for him by the referee in bankruptcy."

§ 1448. "Judgment" Means Judgment Lien, Not Judgment Itself.

—The "judgment" referred to in § 67f, where the statute invalidates all "judgments" and "other liens," does not refer to judgments where no lien is obtained. It means judgment liens.⁴⁷

⁴⁷ *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165 (reversing *In re Lesser* Bros., 5 A. B. R. 320, C. C. A. N. Y.); *obiter*, *Kinmouth & Braeutigam*, 10 A.

In re Beaver Coal Co., 7 A. B. R. 542, 113 Fed. 889 (C. C. A. Ore., affirming 6 A. B. R. 404, 110 Fed. 630): "Construing the language above quoted from § 67 'f' we think it refers solely to liens, and that it does not mean that all judgments rendered within four months prior to bankruptcy shall be null and void. The use of the words 'judgments,' and 'or other liens' indicates that it was the purpose of the act to avoid liens only which were obtained by judicial proceedings within the prescribed time, and not to declare void judgments as such. This view is in harmony with other provisions of the Bankruptcy Law. Judgments rendered even after bankruptcy are sustained as determining the claim thereby adjudged."

In re Blair, 6 A. B. R. 206, 108 Fed. 529 (D. C. Mass.): "Section 67f avoids certain liens, if created within four months. This is its object. It does not avoid judgments or levies, except so far as these create a lien."

In re Kavanaugh, 3 A. B. R. 832, 99 Fed. 928 (D. C. Ky.): "This does, indeed, make certain liens and judgments void if obtained within four months of the adjudication; but it appears to us to be evident that the language, properly construed, was intended only to apply to such judgments as of themselves created liens. Liens thus created were intended to be overthrown and made ineffectual by the adjudication in bankruptcy, unless preserved for the benefit of the estate."

"Probably in most of the States of the Union—certainly in many of them—a judgment for debt, particularly if docketed and indexed, creates a lien upon the debtor's property; and we apprehend, from the connection in which the word 'judgment' is used in the paragraph quoted, that it was meant to confine its meaning to that class of judgments. The section in the main relates to liens, although subsection 'e' provides that certain mortgages or transfers made after the passage of the Bankrupt Act shall also be void upon certain conditions therein provided."

"It seems to us that a clear distinction should be drawn between judgment in this sense, upon a debt—a mere personal liability—and a decree of the chancellor declaring the property rights of parties in a case like the one before us, but which in no way created a lien."

Doyle v. Heath, 4 A. B. R. 705, 22 R. I. 213: "Literally construed, again § 67f avoids 'all judgments' against a bankrupt rendered within four months of the filing of the petition, irrespective of the time of the institution of the suit in which the judgment was ordered, and all such judgments are avoided, although no lien or preference was created thereby, for the language is without limitation or exception. But the difficulty and unreasonableness of adopting a literal construction of the words 'all judgments' appear upon considering the effect produced upon other sections of the act, and upon other provisions of the United States statutes concerning judgments. In the first place, the words are found in the act under the subtitle 'Liens,' and they are conjoined with 'levies, attachments or other liens.' Again, under § 63a of the act the debts which may be proved against a bankrupt are defined as including '(1) a fixed liability, as evidenced by a judgment or an instrument in writing absolutely owing at the time of the filing of the petition against him;' and this without restriction as to the date of entry of the judgment. And § 63 (5) also includes debts 'founded

B. R. 85, 52 Atl. 226 (N. J. Ch.); In re Bailey, 16 A. B. R. 290, 144 Fed. 214 (D. C. Ore.); In re Pease, 4 A. B. R. 550 (Ref. N. Y.); compare, analogously, Owen v. Brown, 9 A. B. R. 717, 120 Fed. 812 (C. C. A. Colo.). See editor's

note to In re Beaver Coal Co., 5 A. B. R. 787 (D. C. Ore.). Compare, to same effect, analogously, In re Chapman, 3 A. B. R. 607 (D. C. Ga.). See (1867) Catlin v. Hoffman, 9 N. B. Reg. 345.

upon provable debts reduced to judgment after the filing of the petition.' Under § 17, among debts not affected by a discharge are '(2) judgments in actions for fraud or obtaining property by false pretenses or false representations, or for willful and malicious injury to the person or property of another'—a manifest inconsistency if the words 'all judgments' are to be taken literally. Again, § 905, Rev. St. U. S., provides that 'the records and judicial proceedings of the courts of any State or Territory when duly authenticated as therein specified, shall have such faith and credit given to them in every court in the United States as they have by law or usage in the courts of the State from which they are taken. And it is hardly to be supposed that this general provision of federal legislation, first substantially enacted in 1790, was intended to be repealed by the single addition of the word 'judgments' in this clause of the Bankrupt Act of 1898. And, if the words 'all judgments' are to be literally construed, they must include judgments rendered in the courts of foreign countries, irrespective of treaty stipulations, and even the judgments of the very court in which the estate of the bankrupt is being administered. We decline to adopt such a construction of the language of the act, and we construe the words 'all judgments' to be qualified and defined by their context, and to be limited to the lien or preference created by such a judgment."

And it means liens by way of levy of execution or attachment, or by way of creditor's bill under judgment.⁴⁸

§ 1449. Judgments Whose Liens Annulled Yet Valid for Other Purposes, as *Res Adjudicata*, etc.—A judgment whose lien is thus annulled may yet be valid so far as it fixes the extent and validity of the claims involved; and may even be *res judicata* as to the fraudulent character or otherwise of transfers therein sought to be set aside.⁴⁹

Metcalf v. Barker, 9 A. B. R. 36, 187 U. S. 44: "Moreover other provisions of the act render it unreasonable to impute the intention to annul all judgments recovered within four months. By § 63a, fixed liabilities evidenced by judgments absolutely owing at the time of the filing of the petition, or founded upon provable debts reduced to judgments after the filing of the petition and before the consideration of application for discharge, may be proved and allowed, while under § 17 judgments in actions of fraud are not released by a discharge, and other parts of the act would be wholly unnecessary if § 67f must be taken literally."

In *re Lesser Bros.*, 5 A. B. R. 320 (C. C. A. N. Y., affirming 3 A. B. R. 815, reversed on other grounds, in *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165): "In this case, it is not necessary to say that the entire judgment is null and void, because the judgment was to the effect that the transfers and assignments of personal property and the receiverships were fraudulent and void, and this part of the judgment is not affected by the Bankrupt Act. The lien, however which was created by the judgment has become discharged by the

⁴⁸. *Bear v. Chase*, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S. C.); In *re Darwin*, 8 A. B. R. 703 (C. C. A. Tenn.); In *re Lesser Bros.*, 5 A. B. R. 320 (C. C. A. N. Y., reversed, on other grounds, sub nom. *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165); In *re Matthews & Son*, 20 A. B. R. 570, 163 Fed. 127 (D. C. N. Y.).

⁴⁹. *Obiter*, In *re Beaver Coal Co.*, 7 A. B. R. 542, 113 Fed. 889 (C. C. A. Ore.), quoted ante, at § 1448. *Obiter*, *Doyle v. Heath*, 4 A. B. R. 705, 22 R. I. 213. *Contra*, *St. Cyr. v. Daignault*, 4 A. B. R. 638, 103 Fed. 854 (D. C. Vt.).

provisions of § 67, and the Metcalfs cannot have the benefit of the decree which directs payment to them of their judgments in the actions at law because the preference created by the decree was made null by the bankrupt Act."

In re Pease, 4 A. B. R. 547 (Ref. N. Y.): "The word 'judgment' is found in a section captioned by the word 'Liens,' and given over to that subject alone. It is apparently limited by the succeeding words, 'or other liens,' and the words, 'the property affected by the levy, judgment, attachment or other lien shall be deemed wholly discharged and released from the same.' Further, by § 63a (1) and (4), judgments are provable debts; while, if all judgments against an insolvent within four months are void, some of the words in § 60a, defining preferences, would be nonsense. An examination of § 3a (3) and § 17a (2) will further demonstrate the weakness of the contention.

"The word 'judgment' is necessary in this clause. Judgments become liens on realty without a levy or other proceeding. Accurately expressed, the judgment is one thing and the lien another; correctly, a judgment so a lien is a judgment lien. This is what is meant by the statute. Had the word 'judgment' been omitted, judgment liens, unlike other liens, might perhaps have been held good, even if against an insolvent and within the four months."

Expressive but obiter, *Kinmouth v. Braeutigam*, 10 A. B. R. 85 (N. J. Ch.): "The sentiment of the Federal courts seems to be that § 67, par. 'f,' applies only to the lien of judgments, and not to the judgments themselves. The judgment itself may remain until it is ascertainable whether the bankrupt will or will not be discharged. In case of a discharge of the bankrupt, the judgment is released. In case of the failure of the bankrupt to obtain his discharge, the judgment remains. But even in the latter event it can never be enforceable against any property owned by the bankrupt at the time he filed his petition in bankruptcy, but can only be used against after-acquired property. This view in respect to the entry of a judgment after the filing of the petition in bankruptcy, as well as in regard to the force of such judgment as a lien, is supported by the provisions of § 63, par. "a," subd. 5, of the Bankrupt Act. Debts of the bankrupt may be proved and allowed against his estate which are founded upon provable debts reduced to judgment after the filing of the petition, and before the consideration of the bankrupt's application for discharge, less costs incurred and interest accrued after the filing of the petition, and up to the time of the entry of such judgment. Here is a recognition of judgments entered between the filing of the petition and the application for discharge; while the provision respecting the provability of debts so reduced to judgment, less costs and interest accrued after the filing of the petition, is an implied negation of the existence of any lien to be obtained in any manner against the bankrupt's property by force of such judgment."

And while § 67f discharges the lien of an attachment, it does not vacate the writ.⁵⁰

§ 1450. Lien by Legal Proceedings May Have Been Indirectly Effected.—The appropriation may be effected indirectly by the legal proceedings. Thus the property of the bankrupt may be discharged from the attachment levy by the giving of a redelivery bond, but if the bankrupt has pledged property of the estate to indemnify the surety on the redelivery

50. *King v. Block Amusement Co.*, 20 A. B. R. 784, 126 App. Div. 48, 111 N. Y. Supp. 102, quoted at § 1447, cited in *In re Squiers*, 21 A. B. 346, 165 Fed. 515 (D. C. N. Y.).

bond, it is the same as if the attachment lien still subsisted on the bankrupt's property.⁵¹

§ 1450¹₂. **Lien on Property in Foreign Country.**—Where the creditor has obtained a lien by legal proceedings upon the bankrupt's property in foreign countries, such creditor will not be allowed to share in the dividends until he has surrendered the lien.⁵²

In *re Pollmann*, 19 A. B. R. 474, 156 Fed. 221 (D. C. N. Y.): "Inasmuch as there is no evidence of insolvency on Pollmann's part in November, 1904, the referee has based his finding entirely on § 67c (3), * * * holding that the German procedure was of the nature of 'an attachment upon *mesne process*,' that it was begun 'within four months before the filing of a petition in bankruptcy' against Pollmann, and that such lien (i. e., attachment) 'was sought and permitted in fraud of the provisions of this act.' In the able opinion filed by the referee I concur. If the procedure above outlined had taken place, as it well might, in the United States, it cannot be doubted that the successful attachment creditor would have been obliged to refund the proceeds of his attachment. * * * The fact that the lien was obtained in a foreign country can make no difference in the meaning of the phrase 'in the fraud of the provisions of this act.' That expression does not necessarily mean active fraud or illegality, but intent to prevent equitable distribution of the debtor's property, and where that intent obtains is immaterial. But, further, the decision is in my opinion right upon broad equitable grounds. It may well have been that the trustee acquired no title whatever to the German realty. *Oakey v. Bennett*, 11 How. 33, * * *. But this proves no more than that Klemm was entitled to enjoy in Germany the fruits of his German legal proceedings."

§ 1451. **Third Element to Nullify Lien.**—The lien must have been obtained within the four months preceding the filing of the bankruptcy petition.⁵³

51. Impliedly, In *re Eastern Commission & Importing Co.*, 12 A. B. R. 305, 129 Fed. 847 (D. C. Mass.); *obiter*, *King v. Block Amusement Co.*, 20 A. B. R. 784, 126 App. Div. 48, 111 N. Y. 102, quoted at § 1447.

Instance of indirect effecting of lien, *Klipstein v. Allen Miles*, 14 A. B. R. 15, 136 Fed. 385 (C. C. A. Ga.): Surety not indemnified but released because garnishment was within four months and therefore liability on the surety's bond fell with fall of lien.

Instance of indirect effecting of lien: *Hill v. Harding*, 107 U. S. 631.

52. Compare, ante, § 1294¹/₂.

53. *Clark v. Larremore*, 9 A. B. R. 476, 188 U. S. 486, affirming In *re Kenney*, 5 A. B. R. 355, 105 Fed. 897 (distinguished, on other points, in In *re Andre*, 13 A. B. R. 135, C. C. A. N. Y.). In *re Richards*, 3 A. B. R. 145, 96 Fed. 935 (C. C. A. Wis., affirming 2 A. B. R. 518). In *re Kenney*, 5 A. B. R. 355, 105 Fed. 897 (C. C. A. N. Y., affirming 3 A. B. R. 353 and 2 A.

B. R. 494, and itself affirmed sub nom. *Clark v. Larremore*, 9 A. B. R. 476, 188 U. S. 486); *Dunn Salmon Co. v. Pillmore*, 19 A. B. R. 172 (N. Y.), quoted on other point at § 1439. *Batchelder & Co. v. Wedge*, 19 A. B. R. 268, 80 Vt. 353; *obiter*, *Woods v. Klein*, 22 A. B. R. 722, 223 Pa. St. 257, quoted on other points at § 1444; In *re Koslowski*, 18 A. B. R. 723, 153 Fed. 823 (D. C. Pa.).

In *re Collins*, 2 A. B. R. 1 (Ref. Iowa): But this case is not to be considered as authority in so far as it lays down the rule that the lien must have created a preference.

Philmon v. Marshall, 11 A. B. R. 180, 116 Ga. 811, where the court introduces the further element of proof of the claim in the bankruptcy proceedings, holding that "a discharge does not affect the lien of a creditor who did not prove his debt in the bankruptcy court when the lien was created more than four months preceding the filing of the bankruptcy

Metcalf v. Barker, 187 U. S. 165, 9 A. B. R. 36: "When it is obtained within four months the property is discharged therefrom but not otherwise."

Compare, to same effect, *In re Dunavant*, 3 A. B. R. 41 (D. C. N. Car.): "A proceedings in bankruptcy does not affect liens accruing four months prior to petition filed."

Keystone Brew. Co. v. Schermer, 31 A. B. R. 279, 241 Pa. 361: "It will be noticed that under this section, two things are required in order to render the lien void: First, it must have been entered within four months prior to the filing of the petition in bankruptcy." [This case quoted further at § 1460.]

And it is not the date of the sale under the lien that is to be taken but the date the lien becomes attached.

Owen v. Brown, 9 A. B. R. 717 (C. C. A. Colo.): "The date of the sale is immaterial, whenever it took place it had relation back to the date the lien of the judgment attached."

petition." The decision is correct, but there seems to be an unnecessary reference to the discharge and also to the filing of proofs of claim. The lien if void at all would not be void by virtue of the discharge nor of the filing of a proof of claim but simply by virtue of the provisions of the law annulling liens on adjudication of bankruptcy.

Also, see *In re Snell*, 11 A. B. R. 35, 125 Fed. 154 (D. C. Calif.); *Levor v. Seiter*, 5 A. B. R. 576 (N. Y. Sup. Ct., reversed, on other grounds, in 8 A. B. R. 459); *In re Engle*, 5 A. B. R. 372, 105 Fed. 893 (D. C. Penn.); *In re Francis-Valentine Co.*, 2 A. B. R. 188, 94 Fed. 793 (D. C. Calif., affirmed in 2 A. B. R. 522, 93 Fed. 953); *In re Blumberg*, 1 A. B. R. 633, 94 Fed. 476 (D. C. Tenn.).

In re English, 10 A. B. R. 133 (D. C. N. Y., reversed in 11 A. B. R. 674, 127 Fed. 940): "In the case at bar, an equitable lien upon partnership assets was created by the transfer of the interest in the partnership estate more than four months prior to the filing of the petition. Subsequently such lien, by decree of the State court, was reaffirmed, and became an established liability, which had accrued previously, and prior to the four months' period. This interest was paramount to the rights acquired by the trustee in bankruptcy to the funds in the hands of the receiver. It therefore follows that jurisdiction of the State court over the partnership property of the bankrupts was not divested by the proceedings in bankruptcy." This case was reversed in 11 A. B. R. 674 as far as it concerned the refusal of the bankruptcy court to order the State court receiver to turn over the balance in his hands to the trustee rather than to distribute it to creditors it-

self. The reviewing court also criticizes the designating of the rights of the transferee as being by way of "an equitable lien." The case was simply that of a payment of a firm creditor by the partnership's transfer of part of its assets more than four months before bankruptcy; the institution of proceedings for dissolution and winding up, culminating in an order entered within four months of subsequent bankruptcy finding the transferee to be a tenant in common—and also to have an equitable lien thereby—and also endeavoring to make distribution among creditors—the latter part of the order being the objectionable part.

Obiter, *In re Bailey*, 16 A. B. R. 291, 144 Fed. 214 (D. C. Ore.); *In re Kavanaugh*, 3 A. B. R. 832, 99 Fed. 928 (D. C. Ky.).

Compare, *Owen v. Brown*, 9 A. B. R. 717 (C. C. A. Colo.): This case was concerned with a preference by legal proceedings as an act of bankruptcy yet lays down the broad principle that "No provision of the Bankruptcy Act of 1898 contemplates that valid judgment liens on real property acquired before the passage of the act or more than four months before the filing of the petition shall be vacated or that the due enforcement of such liens by execution shall constitute an illegal preference."

Compare, analogously, *In re Heckman*, 15 A. B. R. 501 (C. C. A. Wash.); impliedly, *In re S. Oh. Mi.*, 18 A. B. R. 138 (D. C. Hawaii); *In re Arden*, 26 A. B. R. 684, 188 Fed. 475 (D. C. N. Y.); *Keystone Brewing Co. v. Jacob Schermer*, et al 31 A. B. R. 279 (Sup. Ct. Penna.); instance, *In re Randolph*, 26 A. B. R. 623, 187 Fed. 186 (D. C. W. Va.).

§ 1452. If Obtained after Filing of Petition, Not Nullified by § 67 "f"—Though Perhaps Otherwise Void.—Liens obtained by legal proceedings after the filing of the bankruptcy petition are not nullified by § 67 "f," though they may be void for other reasons; for § 67 "f," relating to liens by legal proceedings, unlike § 60 (a), relating to preferences, does not affect liens obtained after the filing of the petition.

Kinmouth v. Braeutigam, 4 A. B. R. 345, 46 Atl. (N. J.) 769: "It is argued on behalf of the motion that the words, 'at any time within four months prior to the filing of a petition in bankruptcy,' mean at any time after a date that is four months prior to the filing of the petition, even although the lien is obtained subsequent to such filing. I cannot assent to this construction. The words are perfectly plain, and have no inclusion of a judgment obtained after the filing of the petition. The way to prevent judgment in a pending action is to stay the suit until the adjudication in bankruptcy, and a sufficient time afterwards to afford opportunity, to obtain and plead a discharge. Possibly, if default be made, the court will, upon discharge being granted, open the judgment in order to allow it to be pleaded; but it will not vacate a judgment regularly obtained, because of the possibility of a subsequent discharge."

Kinmouth v. Braeutigam, 10 A. B. R. 85, 52 Atl. (N. J.) 226: "Being entered not within four months preceding the filing of the petition in bankruptcy, but after the filing of the petition, it was not successfully challenged on a motion to vacate it."

In *re Engel*, 5 A. B. R. 372 (D. C. Pa.): "It has been recently decided in *St. Cyr v. Daignault* that a judgment by default taken since adjudication is void, and that a permanent stay of proceedings should be granted. I have no doubt that the grant of a permanent stay was right, but, with great respect for the opinion of the learned judge who decided that case, I find myself, unable to agree with the reason given therefor. I do not think that clause 'f' of § 67 applies to judgments entered after the adjudication. It seems clear to me that this clause refers entirely to judgments and other liens obtained within four months preceding the filing of the petition; and, indeed, I do not find any provision in the act dealing with the lien of judgments entered after the proceeding in bankruptcy has been begun. The reason for this apparent omission may be found in the fact that § 70 expressly provides that, after the trustee has been appointed, the title to the bankrupt's property shall vest in him as of the date of the adjudication; and while it is true that during the interval between the adjudication and the appointment of the trustee the title to the property remains in the bankrupt, it is a title liable to be divested upon the appointment of a trustee, and a title upon which no permanent lien can be acquired. It may have been thought unnecessary, therefore, to pay any attention to what must be an unavailing effort to obtain a lien."

§ 1453. Whether Lien Obtainable by Legal Proceedings after Filing Bankruptcy Petition.—It has been broadly stated that no lien can be obtained by legal proceedings on the bankrupt's property after the filing of the petition, neither before adjudication,⁵⁴ nor after adjudication, al-

⁵⁴ *Kinmouth v. Braeutigam*, 10 A. B. R. 83, 52 Atl. 226 (N. J.); *Kinmouth v. Braeutigan* 4 A. B. R. 344 (N. J. Ch.); *State Bk., v. Cox*, 16 A. B. R. 32, 143 Fed. 91 (C. C. A. Ills.);

compare, *In re Engle*, 5 A. B. R. 372, 105 Fed. 893 (D. C. Penn.).

It would seem on principle that liens by legal proceedings obtained before the passage of the Bankrupt Act

though before a trustee is appointed.⁵⁵

But this inability does not arise through the prohibitions of § 67 (f) as we have seen in the preceding paragraph; although, as we have also seen, preferences may be created by the act of the bankrupt after the filing of the petition if before adjudication, and may be created even by way of legal proceedings.⁵⁶ But it arises from the fact that the assets are already sequestrated in the bankruptcy court and that a seizure thereof by another court is consequently prohibited.⁵⁷

§ 1454. Computation of Time.—The time is to be computed by excluding the day the act was committed and including the day the petition was filed;⁵⁸ and it is held that fractions of a day are not to be considered.⁵⁹

§ 1455. Attachment or Other Lien Effected before Four Months, but Judgment Not Rendered until within, Lien Good.—Where an attachment or execution is levied or the summons upon a creditor's bill served more than four months before the debtor goes into bankruptcy, the lien thus obtained is not annulled, although the judgment or decree determining it to be proper may not be rendered until within four months before the bankruptcy.⁶⁰

would not be affected. And it has been held, indeed, that a creditor's action begun before the passage of the Bankruptcy Act is not abated. *Nat'l Bk. v. Hobbs*, 9 A. B. R. 190, 118 Fed. 626 (U. S. C. C. Ga.). But compare the following cases: *Owen v. Brown*, 9 A. B. R. 717, 120 Fed. 812 (C. C. A. Colo.); *Nat'l Bk. of The Republic v. Hobbs*, 9 A. B. R. 190, 118 Fed. 626 (C. C. A. Ga.); contra, analogously, *In re Brown*, 1 A. B. R. 107 (D. C. Ore.); *In re Adams*, 1 A. B. R. 94 (Ref. N. Y., distinguished in *re Meyers*, 1 A. B. R. 352). These cases could all be equally as well decided on the four months limitation since they are instances in all cases where bankruptcy did not occur within the four months.

^{55.} *In re Engle*, 5 A. B. R. 372, 105 Fed. 893 (D. C. Penn.); *St. Cyr. v. Daignault*, 4 A. B. R. 638, 103 Fed. 854 (D. C. Vt.).

^{56.} See definition of preference in *Bankr. Act*, § 60 (a).

^{57.} Compare doctrine of § 1270 9/10, "Maxim That Filing of Petition a Caveat, Attachment and Injunction." Inferentially, *State Bk. v. Cox*, 16 A. B. R. 32, 143 Fed. 91 (C. C. A. Ills.): "It is sufficient to remark that the alleged cause of action does not rest upon the provision relating to preferences, but upon the prohibited seizure and appropriation of property of the estate vested in the

court of bankruptcy for administration." Compare, to same effect, *In re Engle*, 5 A. B. R. 372, 105 Fed. 893 (D. C. Penn.).

^{58.} *Bankr. Act*, § 31; *Dutcher v. Wright*, 94 U. S. 553; *In re Dupree*, 97 Fed. 28; *In re Stevenson*, 2 A. B. R. 66, 94 Fed. 110 (D. C. Del.); *In re Planing Mill Co.*, 6 A. B. R. 38 (Ref. N. Y.); *Jones v. Stevens*, 5 A. B. R. 571, 48 Atl. 170 (Sup. Jud. Ct. Me.). See *Leidigh Carriage Co. v. Stengel, et al.*, 95 Fed. 637 (C. C. A. Ohio). Compare, ante, § 1375.

^{59.} *In re Warner*, 16 A. B. R. 519 (D. C. Conn.); *In re Planing Mill Co.*, 6 A. B. R. 38 (Ref. N. Y.); *Jones v. Stevens*, 5 A. B. R. 571, 48 Atl. 170 (Sup. Jud. Ct. Me.). Compare (analogously—fraudulent conveyance under § 67 [e]), *In re Hill*, 15 A. B. R. 499 (D. C. Calif.). Contra, *Manufacturing Co. v. Grant*, 60 Me. 88. It is the date of the filing of the petition, not of the issuance nor service of the subpoena that controls. *In re Lewis*, 1 A. B. R. 458 (D. C. N. Y.).

^{60.} *In re Blumberg*, 1 A. B. R. 633, 94 Fed. 476 (D. C. Tenn.).

Pepperdine v. Bk. of Seymour, 10 A. B. R. 570 (Court of Appeals St. Louis): "Under the interpretation of the statutory provisions by the courts of this State a specific lien is secured from the moment of levy by attachment upon the property seized, ma-

The lien itself was obtained when the levy was made—the subsequent decree simply established the fact that it was rightly obtained.

Metcalf v. Barker, 9 A. B. R. 36, 187 U. S. 165 (reversing *In re Lesser Bros.*, 5 A. B. R. 320, which in turn had affirmed 3 A. B. R. 185): "In our opinion the conclusion to be drawn from this language is that it is the lien created by a levy, or a judgment, or an attachment, or otherwise, that is invalidated, and that where the lien is obtained more than four months prior to the filing of the petition, it is not only not to be deemed to be null and void on adjudication, but its validity is recognized. When it is obtained within four months the property is discharged therefrom, but not otherwise. A judgment or decree in enforcement of an otherwise valid pre-existing lien is not the judgment denounced by the statute, which is plainly confined to judgments creating liens. If this were not so the date of the acquisition of a lien by attachment or creditor's bill would be entirely immaterial.

"Moreover other provisions of the act render it unreasonable to impute the intention to annul all judgments recovered within four months.

"By § 63a, fixed liabilities evidenced by judgments absolutely owing at the time of the filing of the petition, or founded upon provable debts reduced to judgments after the filing of the petition and before the consideration of application for discharge, may be proved and allowed, while under § 17 judgments in actions of fraud are not released by a discharge, and other parts of the act would be wholly unnecessary if § 67f must be taken literally."

tured by the judgment, and the execution thereunder relates back to the time of the levy, so that a sale thereunder passes a title divested and discharged of all succeeding incumbrances. The lien is created by the attachment levy, and bears date thereof, but is fixed by the judgment."

Colston v. Austin Run Mining Co., 28 A. B. R. 92, 194 Fed. 929, (C. C. A. Del.), quoted ante, § 1384½; *Nat'l Bk. v. Moses*, 11 A. B. R. 772 (Sup. Ct. N. Y.); *In re Beaver Coal Co.*, 7 A. B. R. 542, 113 Fed. 889 (C. C. A. Ore., Affirming 6 A. B. R. 404); *Owen v. Brown*, 9 A. B. R. 717, 120 Fed. 812 (C. C. A. Colo.); *In re Blair*, 6 A. B. R. 206, 108 Fed. 529 (D. C. Mass.); *In re Chapman*, 3 A. B. R. 607, 99 Fed. 395 (D. C. Ga.); *In re Frazier v. Trust Co.*, 3 A. B. R. 710, 99 Fed. 707 (C. C. A. N. Car.); *In re Kavanaugh*, 3 A. B. R. 832, 99 Fed. 928 (D. C. Ky.); *Pickens v. Dent*, 5 A. B. R. 644, 106 Fed. 653 (C. C. A. W. Va.); impliedly, *Bank v. Katz*, 1 A. B. R. 19 (Superior Ct. Ills.); impliedly, *Reid v. Cross*, 1 A. B. R. 34 (Superior Ct. Ills.); *Taylor v. Taylor*, 4 A. B. R. 211, 59 N. J. Eq. 86; *Doyle v. Heath*, 4 A. B. R. 705, 22 R. I. 213; *In re U. S. Graphite Co.*, 20 A. B. R. 573, 159 Fed. 300, 161 Fed. 583 (D. C. Pa.); *Nat'l Surety Co. v. Medlock*, 19 A. B. R. 654, 2 Ga. App. 665, 58 S. E. 1131.

Compare, analogous proposition ante, § 1444.

In re De Lue, 1 A. B. R. 387, 91 Fed. 510 (D. C. Mass.): But perhaps this case is based rather on the error that 67 "f" applies only to involuntary bankruptcies. Compare, *Peck Lumber Mfg. Co. v. Mitchell*, 1 A. B. R. 701, 95 Fed. 258 (Com. Pleas Pa.). Compare, *Bank v. Elliott*, 6 A. B. R. 409, 85 N. W. 417. Compare, analogously, *In re English*, 10 A. B. R. 133 (D. C. N. Y.). In this case the lien was created more than four months prior to the filing of the petition in bankruptcy, not by legal proceedings, but by the transfer of an interest in the partnership estate.

But in some States the lien has been held as not attaching until judgment. In such States a contrary rule, therefore, would obtain; thus as to creditor's bills; and thus as to attachments: *In re Lesser*, 5 A. B. R. 326, 108 Fed. 201 (C. C. A. N. Y., disapproved in *In re Blair*, 6 A. B. R. 206, 108 Fed. 529, and reversed by U. S. Sup. Court in *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165); *In re Johnson*, 6 A. B. R. 202, 108 Fed. 373 (D. C. Vt.); *In re Tobias Lesser*, 5 A. B. R. 326 (D. C. N. Y.).

Perhaps these latter cases are also to be considered as overruled by *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165.

Such is the rule where the attachment or garnishment itself is superseded by the giving of a redelivery bond, the bond taking the place of the property.^{60a}

Nat'l Surety Co. v. Medlock, 19 A. B. R. 654, 2 Ga. App. 665, 58 S. E. 1131: "Whether the service of a summons of garnishment creates a technical lien on the funds in the hands of the garnishee or not, still, especially when the garnishee admits liability and pays the fund into court, or in lieu of such actual payment a statutory bond is substituted, the court acquires such a hold upon the money or the res, such a right to retain and administer the fund, or what has been substituted for the fund, the bond, that the subsequent adjudication in bankruptcy, made more than four months thereafter, will not disturb it."

And the rule is the same where the sheriff sells the property and holds the proceeds to await final judgment.

In re Crafts-Riordan Shoe Co., 26 A. B. R. 449, 185 Fed. 931 (D. C. Mass.): "While the sale might have been prevented by giving bond to dissolve the attachment, it cannot be said that any 'preference' obtained by the attachment, would have been vacated or discharged by such a bond, which would have left the plaintiffs in full possession of any advantage over other creditors which their attachment may have given them."

Similarly, where within the four months, a receiver was appointed in proceedings supplementary to execution which had been instituted before the four months, the lien was held to revert to the date of the order in the supplementary proceedings, not to the date of the appointment of the receiver.

Wrede v. Clark, 21 A. B. R. 821 (N. Y. Sup. Ct., App. Div., reversing 21 A. B. R. 170): "The question for determination is whether the service of the order in supplementary proceedings upon the judgment debtor prior to the four months' period created a lien upon his property rights in the seat on the Stock Exchange, so that if the trustee in bankruptcy took anything he took it subject to such lien; or whether, although the plaintiff was appointed and qualified as receiver during the four months' period, his title to the judgment debtor's rights in the seat related back to the commencement of the proceedings instituted by service of the order on the judgment debtor, so that no title whatever passed to the trustee in bankruptcy. We are of the opinion that a lien was created as of the commencement of the proceedings and that the surplus being insufficient to pay the judgment represented by plaintiff the trustee in bankruptcy was entitled to no part of it and that all of it should have been awarded to the plaintiff-receiver. Section 2469 of the Code of Civil Procedure prescribes that where a receiver in supplementary proceedings has been appointed and has duly qualified so that title to the property of the judgment debtor shall become vested in him, such title extends back by relation for the benefit of the judgment creditor in whose behalf the special proceedings was instituted to the time of the service of the order for examination, and that such title by relation back to the time of the commencement of the proceedings shall be good as against all per-

60a. *King v. Block Amusement Co.*, 20 A. B. R. 784, 126 App. Div. 48, 111 N. Y. Supp. 102, quoted at § 1447.

sons except a purchaser in good faith without notice and for a valuable consideration or the payment of a debt due the judgment debtor in good faith and without notice. The language of the section is plain and the courts have not attempted to construe it other than literally, but have held that upon the appointment of a receiver in supplementary proceedings and his qualification he takes the legal title to all the personal property of the judgment debtor, whether in his hands or in the hands of others, as of the date of service of the order in supplementary proceedings, except as to purchasers in good faith or a debtor who has paid his debt in good faith. (*Ward v. Petrie*, 157 N. Y. 301, 307.) The commencement of the proceedings supplementary to execution gave the judgment creditor a lien upon the property of the judgment debtor, and that lien having been acquired more than four months prior to the bankruptcy proceedings was not affected thereby."

And where a creditor's petition was begun or levy made before the passage of the Bankruptcy Act, the creditor's bill is not abated nor the lien annulled, although final judgment in the creditor's bill or in the attachment suit, or in the suit to enforce the execution lien, may not be rendered until within the four months or until after adjudication.⁶¹

The same rule has been held to apply to the case of a judgment rendered within the four months upon an award of arbitrators made before the four months, where, by State law, the lien of such judgment reverts to the date of the rendering of the award.⁶²

Likewise, where the attachment is obtained before the four months but judgment is not rendered until after adjudication, the lien is unaffected.⁶³

§ 1456. But Where State Court Attempts Further Distribution.—But where the State court goes further within the four months period than to make effectual the lien obtained by the legal proceedings prior to the four months period, and attempts further distribution of the remaining assets, a different question arises.

Compare, *In re English*, 11 A. B. R. 674, 127 Fed. 940 (C. C. A. N. Y., reversing 10 A. B. R. 133): "As to the residue of the funds, however, in the hands of the state court receiver, the situation is different. The state court judgment has settled the rights of the contending tenants in common, and distributed the property between them. The funds remaining after *Anna English* has had her share are now no longer undivided property of tenants in common, but have been held to belong in severalty to the bankrupts. So much of the judgment of the state court as directs the distribution of these funds of the bankrupts to their creditors is void, being within the four months. Therefore the receiver now holds them only as a custodian temporarily until he can turn them over to the bankrupts. But the trustee in bankruptcy now stands in the shoes of the bankrupts, and it is to him that they should be turned over. And they should be turned over in their entirety, because there is no lien upon them in favor of any creditor which the bankrupt act respects. There is no

⁶¹ *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165.

⁶² *In re Koslowski*, 18 A. B. R. 723, 153 Fed. 823 (D. C. Pa.), quoted at §

1459. But compare, discussion in § 1459.

⁶³ *Batchelder v. Wedge*, 19 A. B. R. 268, 80 Vt. 353.

pretense that any of the 60 creditors had any lien for his claim prior to the judgment of August 5, 1901, and whatever lien that judgment gave him was cut off a week later by the filing of petition and the subsequent adjudication of bankruptcy."

§ 1457. Conversely, Suit Started before but Lien Obtained within Four Months, Lien Falls.—Conversely, where the suit was started before the four months limit, but the attachment was obtained within it, the attachment falls.⁶⁴

In *re Higgins*, 3 A. B. R. 364, 97 Fed. 775 (D. C. Ky.): "There does not seem to me to be any sound reason for supposing that Congress could have intended to refer to anything except the beginning of that part of the proceeding which secured the writ under which there was a seizure of, and consequent lien upon, some of the debtor's property, whereby it was put in a position where other creditors could see that a lien was being claimed upon it to the exclusion of their otherwise equal right to share in it."

§ 1458. Likewise Levy within Four Months on Judgment Rendered before, Annulled.—And a levy of execution within the four months upon a judgment rendered before the four months, is also annulled;⁶⁵ unless the judgment itself was a lien, in which event the execution of the court's judgment might not contravene the provisions of § 67 "f."⁶⁶

§ 1459. State Law Controls as to Nature of Lien, Time Takes Effect, Abandonment, etc.—The law of the State will control as to the nature of the lien (for instance, whether it be a "lien by legal proceedings" or not), the time it takes effect and the facts sufficient to constitute an abandonment or vitiation of it.⁶⁷

64. In *re Friedman*, 1 A. B. R. 511 (Ref. N. Y. since D. J.); *Cook v. Robinson*, 28 A. B. R. 182, 194 Fed. 753 (C. C. A. Alaska.).

65. *Peck Lumber Co. v. Mitchell*, 1 A. B. R. 701 (Penn. Com. Pleas.); In *re S. Ah. Mi.*, 18 A. B. R. 141 (D. C. Hawaii).

In *re Darwin*, 8 A. B. R. 703 (C. C. A. Tenn.): In this case it was held, that the rule of the common law prevailed—that the lien of the execution related back to the teste thereof which is the first day of the term at which the judgment was rendered; but that this fiction might be rejected when necessary to the attainment of justice.

Obiter, possibly contra, In *re Shoemaker*, 7 A. B. R. 437, 112 Fed. 648 (D. C. Va.).

Contra, In *re Collins*, 2 A. B. R. 1 (Ref. Iowa): This case follows the case of *De Lue*, which was based on a misconception of § 67 "f".

Impliedly, contra, *White v. Thompson*, 9 A. B. R. 653 (C. C. A. Ala.).

66. Bankr. Act, § 67 (f); analo-

gously, *Owen v. Brown*, 9 A. B. R. 717, 120 Fed. 812 (C. C. A. Colo.). *Obiter*, impliedly, In *re S. Ah. Mi.*, 18 A. B. R. 141 (D. C. Hawaii).

67. See ante, discussion of nature of trustee's title, § 1139, et seq. As to time it takes effect, inferentially, *Thompson v. Fairbanks*, 13 A. B. R. 437, 196 U. S. 516; In *re De Lue*, 1 A. B. R. 387, 91 Fed. 510 (D. C. Mass.); *Pepperdine v. Bank*, 10 A. B. R. 576 (St. Louis Ct. Appeals).

Obiter, In *re Shoemaker*, 7 A. B. R. 437, 112 Fed. 648 (D. C. Va.): This case, however, was taken up with the question of comity and simply held the rights were to be left to the State Court for determination.

Inferentially, In *re S. Ah. Mi.*, 18 A. B. R. 140 (D. C. Hawaii); contra, In *re Darwin*, 8 A. B. R. 703 (C. C. A. Tenn.). Compare, *Mohr & Sons v. Mattox*, 12 A. B. R. 333, 120 Ga. 962; compare, *Doyle v. Heath*, 4 A. B. R. 705, 22 R. I. 213. Compare, apparently but not really contra, In *re Engle*, 5 A. B. R. 372, 105 Fed. 893 (D. C. Pa.).

As to lien of supplementary proceed-

In *re* Thackara Mfg. Co., 15 A. B. R. 259, 140 Fed. 126 (D. C. Pa.): "The question raised in the present case is whether such a lien, which would be protected if duly prosecuted, has been abandoned or has become vacated, through the action of the lien creditor in issuing an execution, and allowing the same to be retained by the sheriff over a long period of time, under an arrangement with the debtor by which the greater part of the indebtedness was gradually liquidated; subsequent executions being in several cases paid in full.

"If the lien thus obtained, which was valid in its inception, continued to be valid as against other creditors, it is no doubt protected by the Bankrupt Act and the claim must be allowed, but the referee (Richard S. Hunter, Esq.) held it to be invalid under the law of Pennsylvania—by which law it must be judged—and refused to award priority for the unpaid balance of the debt. This ruling is now before the court on review, and its correctness has been vigorously attacked. I am of opinion, however, that the referee was right."

On principle, it would seem that the time of the actual "obtaining" of the judgment lien or of the levy of execution or attachment should control; but the tendency of some decisions bearing upon the point seems to be in the opposite direction, to the effect that it does not necessarily control where the statutes or decisions of the State declare that the lien of a judgment or levy shall revert to the beginning of the term or to the attesting of the writ or to some other date.⁶⁸

Impliedly, In *re* Koslowski, 18 A. B. R. 723, 153 Fed. 823 (D. C. Pa.): "But on the other hand, to the extent that the action is sustained and a judgment recovered within the amount of the award, the lien is carried back to the date of its entry, and takes rank accordingly. First National Bank's Appeal, 100 Pa. 418. This is familiar law, which hardly needs the citation of authorities. The only question is as to how to apply it. It is contended by the trustee and the contesting creditors, as already intimated, that, as the judgment which was secured by the claimant was essential to give effect to the award, and was obtained within four months of bankruptcy, the lien of the award is incapable of enforcement, the judgment being nullified either by those provisions of the Bankruptcy Act (§ 67f) which make void 'all levies, judgments, attachments, or other liens, obtained through legal proceedings, against a person who is insolvent, at any time within four months prior to the filing of a petition in bankruptcy against him;' or by those (§ 60a, b) which prohibit and make voidable a preference of one creditor over another which has been similarly secured. * * * Where a valid lien has been secured more than four months prior to bankruptcy, proceedings to enforce the same do not conflict with the bankruptcy law, and may be instituted and prosecuted to the end, if that is requisite. * * * In the present instance, therefore, the applicant was entirely within his rights in taking judgment as he did by agreement with the bankrupt, and it is immaterial that this was within a few days of the filing of the petition. And the merits having been thereby concluded in his favor, the lien of the judgment is carried back to the award, which being

ings, *Wrede v. Clarke*, 21 A. B. R. 821 (N. Y. Sup. Ct. App. Div.), quoted at § 1455.

Blick v. Nimmo, 30 A. B. R. 770 (Md. Ct. of Appeals).

68. *Rock Island Plow Co. v. Reardon*, 222 U. S. 354, 27 A. B. R. 492, affirming *Reardon v. Rock Island Plow Co.*, 22 A. B. R. 26, 168 Fed. 654 (C. C. A. Ills.).

sustained to its full amount, excepting interest, is binding as of the date of its entry, and must be paid."

Inferentially, but not necessarily supporting the proposition, *In re Fellerath*, 2 A. B. R. 40, 95 Fed. 121 (D. C. Ohio): "The first day of that term of court was on November 1st, 1898, so that the judgment lien dated back to that day, although the sheriff could make no levy on the judgment until January 14, 1899."

But compare, *In re Engle*, 5 A. B. R. 373 (D. C. Pa.): "The bonds accompany and are secured by a mortgage, and it is argued in support of the validity of the executions that the lien of the judgments is carried back by the law of Pennsylvania to the date when the mortgage was recorded, and should, therefore, be considered as if the lien had originated at that time. This may be true for certain purposes, but, under the present circumstances, I must decline to assign a fictitious date to the existence of the lien. It is no doubt true that the bonds are for the same debt that is secured by the mortgage, but the judgments are general judgments, capable of being levied upon any real or personal property belonging to the debtor, as well as upon the property mortgaged, and in all essential respects are like a judgment recovered after trial. Their lien, therefore, must be considered as beginning, if at all, upon the date of entry."

Thus, the lien of supplementary proceedings has been held to revert to the date of the service of the order (anterior to the four months), and not to have arisen at the date of the appointment of a receiver therein, though the latter was appointed within the four months time.⁶⁹

But it has been held that the lien of a levy under an execution on an old judgment upon property acquired by the bankrupt, within the four months period, while insolvent, is void under § 67 "f" of the Bankrupt Act, in a state where the rule of the common law prevails, that the lien of the execution relates back to the test thereof, which is the first day of the term at which the judgment was rendered, although such first day of the term was more than four months before the bankruptcy.⁷⁰

And it would seem on principle that the bankruptcy courts need not, in this particular, adopt the fictions of the State law, since the peculiar title and rights conferred by the Bankruptcy Act for the protection of the insolvent fund are involved.

§ 1460. Fourth Element to Nullify Lien—Insolvency.—The debtor must have been insolvent at the time it was obtained.⁷¹

69. *Wrede v. Clark*, 21 A. B. R. 821 (N. Y. Sup. Ct. App. Div.), quoted at § 1455.

70. *In re Darwin*, 8 A. B. R. 703 (C. C. A. Tenn.).

71. Bankr. Act, § 67 (f); *Simpson v. Van Etten*, 6 A. B. R. 204, 108 Fed. 199 (D. C. Penn.); *Levor v. Seiter*, 5 A. B. R. 576 (N. Y. Sup. Ct., reversed, on other grounds, in 8 A. B. R. 459, 74 N. Y. Supp. 499); incidentally, *Clarke v. Larremore*, 9 A. B. R. 476, 188 U. S. 486; impliedly, *Hardt v. Schuylkill, etc., Co.*, 8 A. B. R. 481, 74 N. Y. Supp. 549; *In re Collins*, 2 A. B. R. 1 (Ref. Iowa): Insolvency, however, admitted by agreement of parties.

As to what constitutes insolvency, "fair valuation," etc., and the time the insolvency is to be taken, see ante, "Sixth Element of a Preference," § 1342, et seq.

Adjudication of Bankruptcy as Proof of Insolvency.—The adjudication of bankruptcy itself is proof of insolvency if based on an act of bankruptcy involving insolvency at the date of the levy, *Levor v. Seiter*, 5 A. B. R. 576, 69 N. Y. Supp. 987 (reversed, on other grounds, in 8 A. B. R. 459, 74 N. Y. Supp. 499). See also, post, § 1776.

In re Friedman, 1 A. B. R. 510 (Ref. N. Y.): "* * * it is essential that

Keystone Brew. Co. v. Schermer, 31 A. B. R. 279, 241 Pa. 361: "It will be noticed that under this section, two things are required in order to render a lien void: First, it must have been entered within four months prior to the filing of the petition in bankruptcy * * *. Second, the judgment must have been entered against a person who was insolvent at the date of its entry. * * * Whether or not the bankrupt was insolvent at the time of the entry of the judgment is a question of fact which has been determined by the referee, and he has found that the judgment debtor was not insolvent when the judgment was entered: It was not therefore void for this reason. If the lien of the judgment on the bankrupt's real estate was valid, and was not avoided by the adjudication in bankruptcy, then his grantee took the land subject to the lien of the judgment, and no action by the trustee in bankruptcy to which the lien creditors were not parties, could affect their rights."

And the burden of proof of the insolvency is on the trustee or other party asserting it.

Keystone Brewing Co. v. Schermer, 30 A. B. R. 279, 241 Pa. 361: "We think, too, that the referee rightly held that the burden of proving the insolvency of the judgment debtor at the date of the entry of the judgment rested upon the party alleging it. On the record the judgment is regular and apparently valid, and it is incumbent on those attacking its validity to establish their allegations by affirmative proof."

§ 1461. Fifth Element to Nullify Lien by Legal Proceedings—Debtor Must Eventually Be Adjudged Bankrupt.—The debtor must eventually be adjudged bankrupt, else the lien is not invalidated.⁷² Thus, before adjudication, the lien is not annulled and no power exists to compel summary surrender of the property levied on, although injunction may issue to preserve the status quo.^{73a} Consequently, a receiver may not, before

the bankrupt should be insolvent at the time the attachment is levied."

Dunn Salmon Co. v. Pillmore, 19 A. B. R. 172, 106 N. Y. 88; inferentially, *Coal Land Co. v. Ruffner*, 21 A. B. R. 474, 165 Fed. 881 (C. C. A. W. Va.); *Keystone Brewing Co. v. Jacob Schermer et al.*, 31 A. B. R. 279 (Sup. Ct. Penn.); *Wise Coal Co. v. Columbia, etc., Co.*, 27 A. B. R. 445 (Ct. App. Div.).

But see curious construction of § 67f, to the effect that if the insolvency occurred at any time within the four months it is sufficient, even though not existing at the time the lien was obtained, as if the clause "at any time" modified merely the insolvency and not the liens by legal proceedings. *Cook v. Robinson*, 28 A. B. R. 182, 194 Fed. 753 (C. C. A. Alaska): "So that the plaintiff in error is precluded by the adjudication to question the insolvency of Robinson at the time of the filing of the petition in bankruptcy, and it does not affect the case that Robinson may not have been insolvent at the time the attachments of Cook were levied. This for the rea-

son that by subdivision "f" of § 67 all attachments levied against a person insolvent at any time within the filing of the petition in bankruptcy are deemed null and void in case the adjudication in bankruptcy is made. * * * Cook's attachment therefore having been rendered null and void by reason of the adjudication in bankruptcy, it was of no further potency to affect or encumber the property of the bankrupt, and it follows that the inquiry as to the insolvency of the bankrupt at the time the attachment was levied was wholly irrelevant and immaterial. It could in no way affect the inefficacy of the attachment so rendered by the adjudication."

Newberry Shoe Co. v. Collier, 25 A. B. R. 130 (Sup. Ct. Va.).

⁷² In *re Greek Mfg. Co.*, 21 A. B. R. 717, 167 Fed. 427 (D. C. Pa.); also, see, impliedly, all other decisions, under this subdivision, since they are all predicated, impliedly at any rate, on adjudication.

^{73a} See post, "On Adjudication, Invalidating of Lien Relates Back, etc.," § 1467.

adjudication, be required summarily to surrender the assets in his hands, though the receivership has been created within the four months preceding the bankruptcy.

Obiter, impliedly, *In re Kernsten*, 6 A. B. R. 519, 110 Fed. 929 (D. C. Wis.): "The further question as to jurisdiction over the assets of the bankrupts, now in the possession of the receiver appointed by the Circuit Court of Calumet County, which is set up in a plea by the answering creditors, is not one affecting the jurisdiction of the court to proceed to an adjudication in bankruptcy, and cannot be raised at this stage of the proceedings, nor in the form here presented. It is true that jurisdiction over the estate of a bankrupt is essential for its due administration under the provisions of the act of Congress, but if the jurisdiction of the bankruptcy court to that end is ultimately questioned, the issue can arise only after bankruptcy is adjudged and a trustee or other custodian is appointed and qualified to take possession."

State ex rel Strohl v. Sup. Ct. of Kings Co., 2 A. B. R. 97 (Sup. Ct. Wash.): "It would seem that a corporation created under the laws of this State should be subject to the chancery jurisdiction of the courts, and that creditors of such corporations should have their ordinary remedies under existing State laws until such corporation is adjudged a bankrupt under the law of Congress and by the proper tribunal. Unquestionably, upon such adjudication the power of the State court to further proceed ceases."

Thus, likewise, liens by legal proceedings upon an individual partner's property obtained by an individual creditor are not nullified, where the partnership is adjudicated bankrupt but the partner is not adjudicated bankrupt as an individual.^{73b}

The lien is not invalidated by the mere filing of the petition. It is null and void only "in case the debtor be adjudged bankrupt."^{73c}

§ 1462. Invalidity of Liens by Legal Proceedings Ultimately Rests on Basis of Preference.—Upon reflection, it becomes evident that the invalidity of such liens rests on almost the same basis as the voidability of preferences.⁷⁴

In re Kenney, 5 A. B. R. 357, 105 Fed. 897 (C. C. A. N. Y., affirmed, on other grounds, in *Clarke v. Larremore*, 188 U. S. 486): "There can be no doubt that it was the intention of Congress by this section to prohibit creditors of a bankrupt from obtaining preferences over other creditors, as the result of any legal proceedings against him, during the period of four months prior to the filing of the petition; and apt words are used to express that intention. The property of the bankrupt is safeguarded against all such proceedings by the provisions that such of them as would ordinarily be liens against such bankrupt

73b. *Contra*, and that assignee of individual may be ordered summarily to surrender assets: *In re Stokes*, 6 A. B. R. 262, 106 Fed. 312 (D. C. Penn.). And this is so notwithstanding the partnership bankruptcy draws in the individual estates of the members even though they be not adjudged bankrupt individually. See analogous proposition under "Preferences," §§ 1291, 1312½; post, § 2266.

73c. Bankr. Act, § 67 "f."

74. Inferentially, compare, *In re Koslowski*, 18 A. B. R. 723, 153 Fed. 823 (D. C. Pa.), quoted partially at § 1459; inferentially, *Dunn Salmon Co. v. Pillmore*, 19 A. B. R. 172, 106 N. Y. 88; impliedly, *Woods v. Klein*, 22 A. B. R. 722, 223 Pa. St. 257, quoted at § 1444.

shall be deemed null and void, and the property wholly discharged and released from the same. A broad and liberal construction of the section should be adopted if necessary to effect this intent, but no strained construction is necessary in the face of language so comprehensive."

First Nat'l Bk. v. Staake, 15 A. B. R. 645, 202 U. S. 141: "If the interest of Baird in this property were sold solely for the benefit of the attaching creditors, it would obviously result in a preference to those creditors over the general creditors of his estate, and in fraud of the Bankruptcy Act, which is designed to secure equality among all creditors."

In re Tune, 8 A. B. R. 291, 115 Fed. 906 (D. C. Ala.): "The main reason for the four months provision was to prevent the race by creditors to seize the estate of the insolvent when it is found that he is in failing circumstances and to prevent the preferences which would follow if liens and attachments were allowed during that period."

In the case of legal liens to be sure, it is not necessary to prove that the judgment lien was obtained by a creditor—as the term creditor is used in bankruptcy—a judgment lien obtained by anyone being equally void; nor is it necessary to prove that the effect of the enforcement of the lien would be to give such a one a greater percentage of his claim than some one else; nor is it necessary to prove the lienholder had reasonable cause for believing anything—beliefs and intents, in short, cutting no figure in considering the invalidity of legal liens.⁷⁵

Yet the theoretical basis of the invalidity of legal liens is the same as that of the voidability of preferences—protection of the trust fund belonging to all the creditors, so that the maxim, "Equality is equity" may have full sway.

In re Richards, 3 A. B. R. 153, 96 Fed. 935 (C. C. A. Wis.): "It asserts the principle that, as between creditors, "equality is equity" and that the race of diligence must cease, with respect to legal proceedings against a person who is insolvent, at the commencement of four months preceding the filing of the petition."

In re Baird, 11 A. B. R. 437 (D. C. Va.): "While the State law gives to diligent creditors who attach a priority of payment—a preference—over those who do not attach, it is beyond dispute that the intent of the Bankrupt Law (except as to rights gained more than four months before the filing of the petition in bankruptcy) is just the reverse. The intent of the latter, except as aforesaid, is to pro rata all available assets, and to prevent any priority of payment being obtained by any creditor within the four months, whether by consent of the debtor or by the diligence of the creditor."

Nevertheless the operation of § 67 (f) is not confined to liens that create preferences.⁷⁶

§ 1463. Clause "f" of § 67 Supersedes Clause "c" Where in Conflict.—Clause "f" of § 67 supersedes clause "c" of the same section,⁷⁷ wherever they are in conflict.

⁷⁵. In re Richards, 3 A. B. R. 145, 96 Fed. 935 (C. C. A. Wis.); In re Baird, 11 A. B. R. 435 (D. C. Va.).

⁷⁶. See ante, this subdivision, paragraph, § 1431.

⁷⁷. Bankr. Act § 67 (c): "A lien created by or obtained in or pursuant to any suit or proceeding at law or in equity, including an attachment upon mesne process or a judgment by con-

In *re Richards*, 3 A. B. R. 145, 96 Fed. 935 (C. C. A. Wis.): "These two subdivisions, 'c' and 'f,' in our judgment, are plainly antagonistic and irreconcilable. The former saves a lien obtained through legal proceedings begun within four months, unless it was obtained and permitted while the debtor was insolvent, or the creditor had reasonable cause to believe such insolvency, or the lien was sought and permitted in fraud of the provisions of the act. The question of the pecuniary condition of the debtor and knowledge upon the part of the creditor are influential in determining the validity of the lien so obtained. But subdivision 'f' is broader in its scope, and avoids all liens obtained through legal proceedings within the time stated against a person who is insolvent, within the meaning of the subdivision, irrespective of knowledge on the part of the creditor of the fact of insolvency, and irrespective of the question whether the obtaining of the lien was in any way suffered and permitted by the debtor. It avoids all liens obtained through legal proceedings against a person who is insolvent within four months before the filing of the petition. We are unable to reconcile these provisions. They are broadly and clearly in antagonism. It is a question, therefore, how they may be reconciled, for that is impossible. The question is, which shall prevail? The rule in such cases is stated by Puffendorf (Potter, *Dwar. St.* [Ed. 1871] p. 132): 'When we meet with a seeming repugnancy in the terms, conjectures are necessary to work out the genuine sense, by reconciling it, if it is possible, to those terms that seem to be repugnant. But, if there be a clear, evident repugnancy, the latter vacates the former. This rule applies to the making of laws, wills and contracts.'

"Under this rule, subdivision 'f' must control, and we find confirmation of the justice of this rule in the history of this act. Two bills in bankruptcy were presented to Congress; one to the Senate and one to the House of Representatives. They were broadly divergent in spirit. One was supposed to be largely in the interest of the creditor; the other largely in the interest of the debtor. Subdivision 'c' of § 67 was contained in the House bill; subdivision 'f' was contained in the Senate bill. The two houses were at disagreement respecting these bills, and the matter was referred to a conference committee of the two houses near the end of the session, resulting in the incorporation into the House bill of subdivision 'f,' which was in the Senate Bill. Mr. Henderson, in presenting the conference report to the House, stated that subdivi-

session, which was begun against a person within four months before the filing of a petition in bankruptcy by or against such person shall be dissolved by the adjudication of such person to be a bankrupt if (1) it appears that said lien was obtained and permitted while the defendant was insolvent and that its existence and enforcement will work a preference, or (2) the party or parties to be benefited thereby had reasonable cause to believe the defendant was insolvent and in contemplation of bankruptcy, or (3) that such lien was sought and permitted in fraud of the provisions of this Act; or if the dissolution of such lien would militate against the best interests of the estate of such person the same shall not be dissolved, but the trustee of the estate of such person, for the benefit of the estate, shall be subrogated to the rights of the holder of such lien and empow-

ered to perfect and enforce the same in his name as trustee with like force and effect as such holder might have done had not bankruptcy proceedings intervened."

In *re Tune*, 8 A. B. R. 285, 115 Fed. 906 (D. C. Ala.); impliedly, *Bear v. Chase*, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S. C.): compare, In *re Hopkins*, 1 A. B. R. 209 (Ref. Ala.), where clause 67 (c) is held to apply to "new" liens created by legal proceedings. Also, for peculiar but erroneous construction, see In *re Collins*, 2 A. B. R. 1 (Ref. Iowa), begun within the four months period while clause 67 (f) applies to liens created within the four months on old proceedings instituted before that time. This construction was rejected: In *re Friedman*, 1 A. B. R. 510 (Ref. N. Y.).

Cook v. Robinson, 28 A. B. R. 182, 194 Fed. 753 (C. C. A. Alaska).

vision 'f,' was incorporated into the bill to strengthen the bill. 31 Congressional Record, pt. 7, p. 6428, June 28, 1898. The confusion results from the omission of the conference committee to modify the language of subdivision 'c,' or to strike it out altogether; but the passage of the bill by the House with subdivision 'f,' contained in it, after this report of the conference committee, must be taken as an indication of the will of the lawmaking power that the provisions of subdivision 'f' shall prevail, notwithstanding anything antagonistic to them previously found in the act. We are of opinion, therefore, under the rule stated, corroborated and justified by the action of Congress, that the provisions of subdivision 'f' must prevail over those of subdivision 'c,' and that all liens obtained through legal proceedings within the time stated against a person who is insolvent, and irrespective of any sufferance or permission thereof by the debtor and of any knowledge by the creditor of the debtor's insolvency, are avoided if that subdivision can be held to apply to voluntary proceedings in bankruptcy, and if another objection, hereinafter considered, is unavailing."

In *re Rhodes*, 3 A. B. R. 380 (D. C. Pa.): " * * * under the rule that when there is a clear and evident repugnancy between the two classes of the same statute, the latter vacates the former."

Since clause "f" covers in great part the same transactions and is broader than clause "c," clause "c" need not be considered here further than simply to observe that the persistence of both these clauses indicates the conflict that wages all through the law between the two different theories that struggled for supremacy in the framing of the law. The first theory—that embodied in clause "c"—introduced the element of intent and knowledge; whilst the other theory—that embodied in clause "f"—cast aside all consideration of the intent with which a preference was given or received and made the result of the transaction the real test, that is to say, made its effect upon the insolvent fund the test—as to whether the shares of the other creditors were going to be made less by the transaction than was proportionate. Clause "c," makes the invalidity depend upon the knowledge of the creditor as to its working a preference, or, at any rate, upon the debtor's "permitting" of the lien.⁷⁸

Nevertheless, clause (c) is not to be entirely disregarded, for it is still part of the statute.⁷⁹

First Nat. Bk. v. Title & Trust Co., 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.). "It has been suggested, however, that §§ 67c and 67f are in such conflict that both of them cannot stand, and that 67f must stand as the later declaration of the legislative will. * * * In so far as 67c is in conflict with 67f, the former is doubtless superseded by the latter section. But, if our construction of 67c is correct, the lien now under consideration was not dissolved by any of its provisions, but, on the contrary, it was preserved, and the trustee, by operation of law and without any intervening court order, subrogated to the rights of the

⁷⁸. In *re Arnold*, 2 A. B. R. 180 (D. Ky.); compare, In *re Burrus*, 3 A. B. R. 296, 97 Fed. 926 (D. C. Va.).

⁷⁹. Compare reference thereto, *First Nat'l Bk. v. Staake*, 15 A. B. R. 642, 202 U. S. 141. This clause, also, is the

basis of the decision in *In re Pollman*, 19 A. B. R. 474, 156 Fed. 221 (D. C. N. Y.), quoted at § 1450½; and in *Coal Land Co. v. Ruffner*, 21 A. B. R. 474, 165 Fed. 881 (C. C. A. W. Va.), quoted at § 1603.

former receiver. Section 67f does not conflict with this view of 67c. Section 67f, like clauses 1, 2, and 3, of the first sentence of 67c, relates only to liens obtained for the benefit of less than all of the bankrupt's general creditors, and not to a lien which benefits all the creditors and the dissolution of which will result in giving priority to particular creditors. A trustee in bankruptcy is not by 67f subrogated by mere operation of law to the rights of a levying creditor. He must obtain an order of court preserving the rights of the levying creditor for the benefit of the bankrupt's estate, as was done in *First National Bank v. Staake*, 202 U. S. 148, 15 Am. B. R. 639. There the Supreme Court, after quoting both 67c and 67f, and without intimating that 67c is superseded by 67f, upheld the lien of an attachment levied on lands which the defendant in attachment had conveyed, and against whom bankruptcy proceedings were commenced within four months after the levy, not for the benefit of the attaching creditor, but for the benefit of the trustee in bankruptcy who thereby acquired priority over the grantee's unrecorded deed."

And it is upon this clause, most reasonably, that the superseding of the custody of the State courts rests in cases of assignments for the benefit of creditors, receiverships, etc.,⁸⁰ and it is rather under this section than under § 67 "f" that such general assignments, receiverships, etc., within the four months, are to be declared null and void as liens by legal proceedings, since § 67 "f" requires insolvency to exist as an essential element to the nullification; whilst § 67 "c" would not so require but would declare such assignments, receiverships, etc., within the four months, absolutely null and void, as being sought and permitted in fraud of the provisions of this Act.⁸¹

And again, it is under this clause that the bankruptcy court has required the surrender of a lien obtained in a foreign country upon property of the bankrupt there, as a prerequisite to the creditor's participation in the bankruptcy here.⁸²

§ 1464. Clause "f" Applies to Voluntary Bankruptcies as Well as to Involuntary.—Clause "f" applies to voluntary bankruptcies as well as to involuntary bankruptcies, notwithstanding it refers in its mere wording only to cases where a petition is filed "against" a person;⁸³ for clause

80. See discussion, post, § 1603, et seq. Compare, *Coal Land Co. v. Ruffner*, 21 A. B. R. 474, 165 Fed. 881 (C. C. A. W. Va.); compare, *First Nat. Bk. v. Title & Trust Co.*, 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.), quoted at § 1603.

81. In re *Gutwillig*, 1 A. B. R. 392, 92 Fed. 337 (C. C. A. N. Y.).

82. In re *Pollman*, 19 A. B. R. 474, 156 Fed. 221 (D. C. N. Y.), quoted at § 1450½.

83. *Peck Lumber Co. v. Mitchell*, 1 A. B. R. 701 (Penn. Com. Pleas); *Brown v. Case*, 6 A. B. R. 744, 61 N. E. 279 (Mass. Sup. Jud. Ct.); *Menneke v. Rosenberg*, 9 A. B. R. 323, 202 Penn. St. 131; In re *Benedict*, 8 A. B. R. 463

(Sup. Ct. N. Y.); In re *Richards*, 2 A. B. R. 518 (affirmed in 3 A. B. R. 145, C. C. A. Wis., 96 Fed. 935); *McKenney v. Cheney*, 11 A. B. R. 54, 118 Ga. 387; *Mohr & Sons v. Mattox*, 12 A. B. R. 332 (Sup. Ct. Ga.); In re *Blair*, 6 A. B. R. 206 (D. C. Mass., disapproving In re *De Lue*, 1 A. B. R. 387, 91 Fed. 510); In re *Vaughan*, 3 A. B. R. 363, 97 Fed. 560 (D. C. N. Y.); In re *Lesser*, 3 A. B. R. 815, 100 Fed. 433 (D. C.); In re *McCartney*, 6 A. B. R. 367, 109 Fed. 621 (D. C.); *Jones v. Stevens*, 94 Me. 582, 48 Atl. 170, 5 A. B. R. 571; obiter, In re *Higgins*, 3 A. B. R. 367 (D. C. Ky.); In re *Dobson*, 3 A. B. R. 420 (D. C. Ills.); In re *Fellerath*, 2 A. B. R. 40, 95 Fed. 121 (D. C. Ohio); In re *Brown*, 1 A. B.

(1) of § 1 says: "A person 'against' whom a petition has been filed shall include a person who has filed a voluntary petition."

§ 1465. Does Not Impair Obligations of Contract nor Divest Vested Rights.—Clause "f" does not impair the obligation of a contract nor divest the attaching creditor of a vested right.⁸⁴

§ 1466. Operates Only on Liens Obtained before Filing of Petition.—Clause "f" avoids only liens obtained before the filing of the petition, and does not affect those sought to be obtained afterwards. The latter are to be reached in other ways, if at all.⁸⁵

In *re Engle*, 5 A. B. R. 372, 105 Fed. 893 (D. C. Pa.): "I do not think that clause 'f' of § 67 applies to judgments entered after the adjudication. It seems clear to me that this clause refers entirely to judgments and other liens obtained within four months preceding the filing of the petition; and, indeed, I do not find any provision in the act dealing with the lien of judgments entered after the proceeding in bankruptcy has been begun. The reason for this apparent omission may be found in the fact that § 70 expressly provides that, after the trustee has been appointed, the title to the bankrupt's property shall vest in him as of the date of the adjudication; and while it is true that during the interval between the adjudication and the appointment of the trustee the title to the property remains in the bankrupt, it is a title liable to be divested upon the appointment of a trustee, and a title upon which no permanent lien can be acquired. It may have been though unnecessary therefore, to pay any attention to what must be an unavailing effort to obtain a lien. A similar view concerning the scope of § 67f has been expressed in the Supreme Court of New Jersey. *Kinmouth v. Breautigam*, 4 Am. B. R. 344, 46 Atl. 769. I have been speaking of voluntary bankruptcy merely. In a case of involuntary bankruptcy a question might be presented concerning the lien of a judgment entered after the filing of the petition, but before the entry of adjudication, and this question I have not considered."

§ 1467. On Adjudication, Invalidating of Lien Relates Back to Inception of Lien.—The invalidity relates back to the inception of the lien, so that, for all purposes, the lien may be said never to have existed.⁸⁶

R. 107, 91 Fed. 359 (D. C. Oregon); In *re Friedman*, 1 N. B. N. 208; *Mfg. Co. v. Mitchell*, 1 N. B. N. 262; *obiter*, *Bear v. Chase*, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S. C.); *Doyle v. Heath*, 4 A. B. R. 705, 22 R. I. 213.

Contra, In *re De Lue*, 1 A. B. R. 387, 91 Fed. 510 (D. C., disapproved in *In re Blair*, 6 A. B. R. 206, and in *Brown v. Case*, 6 A. B. R. 744, Supreme Jud. Ct. Mass.); also, contra, In *re Easley*, 1 A. B. R. 715, 93 Fed. 419 (D. C., disapproved in *Brown v. Case*, 6 A. B. R. 744, Supreme Jud. Ct. Mass.); also, contra, In *re O'Connor*, 95 Fed. 943 (D. C., disapproved in *Brown v. Case*, 6 A. B. R. 744, Supreme Jud. Ct. Mass.); also, contra, In *re Collins*, 2

A. B. R. 1 (Ref. Iowa, disapproved in *McKenney v. Cheney*, 11 A. B. R. 58, 118 Ga. 387). Instance, In *re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa); *Hall v. Chicago, etc., R. Co.*, 25 A. B. R. 53 (Sup. Ct. Neb.).

⁸⁴. *Wood v. Carr*, 10 A. B. R. 577 (Ky. Court of App.).

⁸⁵. Contra, *St. Cyr v. Daignault*, 4 A. B. R. 638, 103 Fed. 854 (D. C. Vt.); compare, *Kinmouth v. Braeutigam*, 10 A. B. R. 83, 63 N. J. Eq. 103; apparent instance, *Evans v. Stalle*, 11 A. B. R. 182 (Minn.). See ante, § 1452.

⁸⁶. *Clarke v. Larremore*, 9 A. B. R. 478, 188 U. S. 486.

Mohr & Sons v. Mattox, 12 A. B. R. 332 (Sup. Ct. Ga.): "The adjudication of the defendant as a bankrupt on a petition filed within four months of the entering of the judgments rendered the judgments null and void, and the nullity and invalidity related back to the time of entry of the judgments, and affected them and all subsequent proceedings."

Thus, a sheriff may not be mulcted by an execution creditor for failure to proceed with diligence to realize upon an execution, where the execution debtor subsequently goes into bankruptcy within the four months, although had he proceeded with diligence, he might have made the money on his execution and safely turned it over to the execution creditor before the bankruptcy.

Mohr & Sons v. Mattox, 12 A. B. R. 333 (Sup. Ct. Ga., distinguishing *Levor v. Seiter*, 8 A. B. R. 459; also, *McKenney v. Cheney*, 11 A. B. R. 54): "The judgment creditor, obtains his lien subject to its being defeated if the defendant is adjudicated a bankrupt upon a petition filed within four months from the entry of judgment. It was not the laches of the sheriff which caused the movants to lose their rights under their judgment, but the bankruptcy law, which nullified their lien."

§ 1468. Lien Absolutely Void and Falls of Itself.—The lien falls of itself and becomes null and void without the necessity of bringing an action to annul it. It is ipso facto void. In other words, it is absolutely void, not simply voidable.⁸⁷

Schmilovitz v. Bernstein, 5 A. B. R. 265 (Sup. Ct. R. I.): "It was conceded in the argument of the case, and it is well settled by adjudications under the Bankrupt Act of 1867, that an attachment on mesne process made within four months before the commencement of proceedings under the United States Bankrupt Act by or against the defendant in an action in a State court was dissolved ipso facto by the bankruptcy proceedings. * * * The provisions of the Act of 1898 have the same effect with respect to attachments by mesne process, and work the dissolution of other specified liens as well."

In *re Tune*, 8 A. B. R. 285, 115 Fed. 906 (D. C. Ala.): "There is no longer any right of possession in the officer of the State Court who then holds merely as bailee for the person rightfully entitled to possession, and becomes a trespasser if he fails to deliver on proper demand."

In *re Beals*, 8 A. B. R. 639, 116 Fed. 530 (D. C. Ind.): "The moment that Thomas C. Beals was adjudged a bankrupt, the statute operated ex proprio vigore to nullify and render void the judgment set up in the answer of the Pennsylvania Company, and to wholly release and discharge the debt due the bankrupt from such judgment. On what principle can this court hold the judgment to be of any force and effect in the face of a valid statute which declares such a judgment to be a nullity? The adjudication under this statute wipes out the judgment of the justice as effectually as though it never existed, and releases and discharges the debt due the bankrupt from the gar-

⁸⁷. In *re Breslauer*, 10 A. B. R. 33, 121 Fed. 910 (D. C. N. Y.); *Mohr & Sons v. Mattox*, 12 A. B. R. 332 (Sup. Ct. Ga.); In *re Richards*, 2 A. B. R. 506 (D. C. N. Car.); In *re Jennings*, 8 A. B. R. 365 (Ref. N. Y.); inferentially, *Bear & Co. v. Chase*, 3 A. B. R. 746, 99

Fed. 920 (C. C. A. S. C.); impliedly, In *re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa); impliedly, In *re Cohn*, 18 A. B. R. 786 (Ref. Calif., affirmed by D. C.); obiter, In *re Smith*, 23 A. B. R. 864, 176 Fed. 426 (D. C. N. Y.), quoted at § 234.

nishee judgment as completely and effectually as would a formal release executed by the judgment plaintiff. In obedience to the positive mandate of the statute, the court must deem the attachment null and void, and the wages due the bankrupt wholly released and discharged from the same. It is too firmly settled to be open to doubt that, if a garnishee pays over money on a void judgment, he must bear the loss. He will not be heard to say that he paid it in obedience to a void judgment after notice and knowledge that the judgment has been rendered null and void by operation of law. The adjudication having rendered the judgment against the bankrupt and the Pennsylvania Company null and void, it must be treated as a nullity whenever and wherever drawn in question, either in a direct or in a collateral proceeding. Here the judgment is drawn in question collaterally, and its nullity results from the subsequent adjudication by this court of Thomas C. Beals as a bankrupt."

Laches, therefore, cannot be urged as against the trustee.

Hardt v. Schuylkill Plush & Silk Co., 8 A. B. R. 479, 69 App. Div. 90, 74 N. Y. Supp. 549: "I know of no laches on the part of the trustee that would make this attachment valid, which is made void by the provision of the Bankrupt Act."

§ 1469. Nevertheless Creditors Not to Sit by, Else Estopped.—Nevertheless it would hardly be the law that creditors could sit by, and, without bringing to the officer's attention the fact of the filing of the bankruptcy petition, permit him to pay over the proceeds of an execution sale to the execution creditor.

§ 1470. Requisite to Bring Situation to Notice of Court or Officer Seeking to Enforce Lien.—However, in practice it will be found that, while it is not necessary to institute an action to annul the lien, it is usually necessary, and is certainly proper, to institute proceedings of some kind, to bring the matter to the notice of the court or officer in charge.⁸⁸

§ 1471. May Come into Court Where Lien Obtained and Ask for Surrender.—Thus, the trustee in bankruptcy may come into the case where the lien was obtained and ask the court there for the surrender of the property.⁸⁹

Hardt v. Schuylkill, etc., Co., 8 A. B. R. 481, 74 N. Y. Supp. 549: "Although by the express provision of the statute the attachment is to be deemed null and void and the property affected by the attachment deemed wholly discharged and released from the same, we agree with the court below that it was the proper practice to apply to the court for an order formally discharging the attachment and releasing the goods of the bankrupt from the levy. Certainly the sheriff could not be required to assume the responsibility of releasing a levy valid but for the adjudication of bankruptcy. It is the duty of the court, upon these facts being called to its attention, to vacate the attachment and remove the lien so

⁸⁸. *Hardt v. Schuylkill Silk Co.*, 8 A. B. R. 481, 74 N. Y. Supp. 549.

Notification of Attaching Officer by Referee.—Instance, *In re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa).

⁸⁹. Instance, *In re Benedict*, 8 A. B. R. 463, 75 N. Y. Supp. 165 (N. Y. Sup. Ct.); impliedly, *In re Hecox*, 21 A. B. R. 314, 164 Fed. 823 (C. C. A. Colo.), quoted at § 1611.

that the trustee in bankruptcy can take the proper proceedings to recover the property of the bankrupt's estate."

In *re Lesser Bros.*, 5 A. B. R. 320 (C. C. A. N. Y., reversed, on other grounds, sub nom. *Metcalf v. Barker*, 187 U. S. 165): "Inasmuch as the fund was in the custody of the State court and had been in such custody prior to the institution of the proceedings in bankruptcy, it was proper to make no order in regard to the action of that court, but to direct the trustee in bankruptcy to apply to it for its order upon the receivers to make payment to him."

The trustee in bankruptcy, also, may come into the case where the lien was obtained and ask the court there for the preservation of the lien of the State court proceedings.⁹⁰

§ 1472. Comity Requires Resort First to Court Wherein Lien Obtained.—Comity requires that resort be first had to the State Court wherein the proceedings involving the lien are pending.⁹¹

Obiter, *Scheyer v. Book Co.*, 7 A. B. R. 390, 112 Fed. 407 (C. C. A. Ga.): "In opposition to the adjudication, it has been very vigorously insisted in this court that the adjudication in bankruptcy should not be rendered, because the State Bankruptcy Court, through its receiver and under the judgment of dissolution, has taken possession of all the property of the corporation, and that by reason of the comity which does and ought to prevail between courts of the States and courts of the United States, the adjudication in bankruptcy can result in no administration or other beneficial effect. For the purposes of this case, we may concur with the learned counsel in his views on this matter of comity, but we are of opinion, notwithstanding, that the petitioning creditors have the right to have their insolvent debtor adjudged a bankrupt, if for no other reason still for the purpose of insisting upon the application of the provisions of the Bankrupt Law annulling preferences in certain cases.

"Section 67f of the act of 1898 reads; * * *

"Even if the State court shall, on proper application, refuse to deliver over the estate of the corporation to the trustee in bankruptcy, which may be properly requested of the State court by the trustee on the ground that, under the Bankrupt Law of the United States, which is paramount to the Insolvency and Liquidation Laws of the State of Alabama, the bankruptcy court has exclusive jurisdiction in the administration and settlement of the bankrupt's estate, still the trustee may intervene in said proceedings in the State court, and pray that the provisions of the Bankrupt Law applicable to the administration of the estate of the insolvent and defunct corporation shall be applied in behalf of the general creditors, and thereby procure a ruling in the State court annulling the preferences herein complained of, or other rulings in harmony with the Bankrupt Laws of the United States."

In *re Hecox*, 21 A. B. R. 314, 164 Fed. 823 (C. C. A. Colo.)—a case of a re-

⁹⁰. See post, § 1489; *Conti v. Sunseri*, 18 A. B. R. 898 (Pa. Com. Pleas).

⁹¹. Impliedly, In *re Shoemaker*, 7 A. B. R. 437, 112 Fed. 648 (D. C. Va.): "Solely on the ground that the State court had acquired jurisdiction of the subject matter of this controversy prior to the institution of the bankruptcy proceedings, comity requires that this

court should decline to enjoin the officer of that court."

Compare, In *re Lengert Wagon Co.*, 6 A. B. R. 535, 110 Fed. 927 (D. C. N. Y.); In *re Hanks*, 2 A. B. R. 634 (D. C. Ala.); impliedly, *Maurau v. Carpet Lining Co.*, 6 A. B. R. 734, 50 Atl. (R. I.) 331; *Wilson v. Parr*, 8 A. B. R. 234, 115 Ga. 629; (1867) *Ex parte Waddell*, Fed. Cas. 17,027.

ceivership created within the four months: "In contemplation of the Bankrupt Act, in so far as concerned his right to the custody of the property of the bankrupt, he stood as if he had never been appointed by the State court. In such situation, as he holds the property not in his own right, but solely in his claimed official capacity, it was his duty, on notification and demand by the trustee in bankruptcy, to deliver the property to him. But inasmuch as he was the appointee of the State court, as a mere act of courtesy, sometimes, but hardly accurately, termed 'judicial comity,' the bankrupt court in the first instance directed the trustee to prefer a request to the State court for an order on its receiver to deliver the property in his custody to the trustee. In such case, if the State court decline to reciprocate the consideration thus paid to its dignity, the law is well settled that it is then competent for, and the duty of, the bankrupt court to order the receiver to deliver the property over to the trustee, and he would be in contempt if he refuse to comply therewith. Controlling authorities affirm the foregoing proposition."

In *re Lesser*, 3 A. B. R. 823, 100 Fed. 439 (D. C. N. Y., reversed, on other grounds, sub nom. *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165): "Although the partnership receivers, under the adjudication in the Court of Appeals, have no legal title to the property, they are still the custodians of it, as officers of the State court appointed in the second equity suit as above stated. The fund is, therefore, in the custody of the State court, and the trustee should apply to that court to make the proper order for the payment thereof by its receiver to the trustee, in whom it is vested by the Bankrupt Act. The obligations of the Bankrupt Act are as binding upon that court as upon this; and it is not to be doubted that on proper application the State court will give appropriate directions."

In *re Kersten*, 6 A. B. R. 516, 110 Fed. 931 (D. C. Wis.): "If the adjudication of bankruptcy so operates, as remarked in the recent decision of the Supreme Court in *Bryan v. Bernheimer* (5 Am. B. R. 623, 629, U. S.), that the property of the bankrupts is 'thereby brought within the jurisdiction of the court of bankruptcy,' it nevertheless rests with the State court, in the first instance, at least, to determine its course when such contingency is duly presented. Moreover, the judicial custody can be changed only through action by the State court for its release, or through plenary procedure, in conformity with the law which governs both jurisdictions, and in accord with comity."

In *re Seebold*, 5 A. B. R. 364, 105 Fed. 910 (C. C. A. La.): "The State court had the amplest possession of the subject of the controversy and full jurisdiction of the parties at the date of the institution of the bankruptcy proceedings. There is no provision in the present bankrupt law which authorizes or permits the courts of bankruptcy, by the use of either summary or plenary process, to stop the proceedings of the State court in a suit in which it had already, before the institution of the proceedings in bankruptcy, obtained possession of the subject matter and jurisdiction of the parties. What effect the provisions of the Bankruptcy Act may have to stay proceedings in a State court is a question of which that court has full jurisdiction to decide, subject to prescribed methods of review, and which the courts of bankruptcy may not attempt to limit or control without a manifest disregard of that comity which is an essential element of our public law, and under which our State and national systems of judiciary work is admirable harmony. Certainly with, and probably without, an order of the court of bankruptcy, the trustee in this case could have made his application to the State court in the suit therein pending, setting up his claim, or the claim of the estate he represents, to the proceeds in question."

Carling v. Seymour Lumber Co., 8 A. B. R. 30, 113 Fed. 483 (C. C. A. Ga.): "When the State court is in possession, through its receiver, of assets that it

is without jurisdiction or authority to hold against a receiver or trustee appointed in bankruptcy proceedings, instead of making a peremptory order on the receiver of the State court to surrender the funds, an injunction, if necessary, might be granted by the bankruptcy court to prevent the unlawful distribution of the assets, until application could be made to the State court for an order to its receiver to surrender the assets to the proper custodian. The laws of the United States being equally binding on all the courts, we cannot assume that the State court would refuse to administer them. We are not now called on to decide what course should be taken in the event of a disregard of the Bankrupt Law by the State court. That such application should be made in the first instance to the State court is sustained, not only by the analogous cases relating to comity, but by adjudications directly in point on this question of practice under the Bankrupt Law."

In re Knight, 11 A. B. R. 1, 125 Fed. 35 (D. C. Ky.): "It would not only be unseemly, but altogether disagreeable, to this court, to pursue any course which would be wanting in the utmost respect and courtesy to the State tribunal, and orders will be made directing the trustee to apply to that court for leave to enter a special appearance in the case there pending, styled 'First National Bank of Fulton v. Henry Knight and others,' for the purpose of filing a copy of this opinion, the orders made in pursuance thereof, a copy of the adjudication in bankruptcy, and an accompanying application for an order of that court directing its receiver to turn over to the trustee in bankruptcy the property of the bankrupt held by the receiver."

And injunction by the Bankruptcy Court will be refused if sought in the first instance;⁹² except perhaps long enough to enable the trustee to apply to the State Court for a surrender.⁹³

And the application to the State court first is not such an election of forum nor is a refusal thereof such a res judicata as to preclude subsequent application to or action by the bankruptcy court.⁹⁴

And the requirement is simply by way of comity, and where an emergency exists, the trustee need not apply first to the State Court, and the bankruptcy court has the right to proceed at once by direct summary proceedings against the court officer.⁹⁵

§ 1473. Bankruptcy Court May Enjoin.—The trustee or other proper party, if any there be, to the bankruptcy proceedings may obtain an injunction.⁹⁶

92. In re Shoemaker, 7 A. B. R. 437, 115 Fed. 648 (D. C. Va.): The court, whilst deciding the case properly, evinces somewhat of a misunderstanding of the principles underlying the avoiding of legal liens in bankruptcy and the jurisdiction of courts of bankruptcy. Compare, In re Lengerdt Wagon Co., 6 A. B. R. 535, 110 Fed. 927 (D. C. N. Y.).

93. Carling v. Seymour, 8 A. B. R. 41, 113 Fed. 483 (C. C. A. Ga.); In re Lengerdt Wagon Co., 6 A. B. R. 535, 110 Fed. 927 (D. C. N. Y.).

94. See post, § 1637. Bear v. Chase, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S.

C.); In re Hecox, 21 A. B. R. 314, 164 Fed. 823 (C. C. A. Colo.). Compare Hooke v. Aldridge, 16 A. B. R. 664, 145 Fed. 865 (C. C. A. Tex.).

95. Analogously, In re Hornstein, 10 A. B. R. 308, 122 Fed. 266 (D. C. N. Y.).

96. In re Kenney, 2 A. B. R. 494, 95 Fed. 427 (D. C. N. Y., affirmed in 3 A. B. R. 353, 5 A. B. R. 355, C. C. A. and reaffirmed sub nom. Clarke v. Larremore, 9 A. B. R. 47, 188 U. S. 486); In re Northrop, 1 A. B. R. 427 (Ref. N. Y.); In re Globe Cycle Wks., 2 A. B. R. 447 (Ref. N. Y.); Blake v. Francis Valentine, 1 A. B. R. 372, 89 Fed. 691 (D. C. Calif.): This case is not ap-

In *re Ransford*, 28 A. B. R. 78, 194 Fed. 658 (C. C. A. Mich.): "The objection, that, by reason of the alleged adverse nature of the claim made by petitioner, the District Court had no jurisdiction to entertain summary proceedings, by way of injunction, cannot be sustained. It follows, from what has been said in the opinion, that the petitioner was not in adverse possession, actual or constructive, of the fund in question. The proceeding in the District Court was a controversy between the trustee in bankruptcy and the petitioner, as to which was entitled to receive payment from the garnisheed defendant of the indebtedness primarily owing to the bankrupt's estate. The rights of a garnishing creditor can be no greater than those of an attaching creditor, and as the rights of the latter are voided by a bankruptcy proceeding, the same must be true of those of the former."

In *re Kimball*, 3 A. B. R. 161 (D. C. Penn.): "Where the personal property of the bankrupt at the date of the adjudication is subject to the levy of a pending execution, the right of this court to enjoin the execution creditor, if the execution is an unlawful preference and contrary to the provisions of the Bankrupt Act, is clear."

Bear v. Chase, 3 A. B. R. 755, 99 Fed. 920 (C. C. A. S. C.): "The power of the United States District Court to enjoin and restrain the parties from the further prosecution of the suits in the State court was plenary, and should have been exercised because necessary to the maintenance of its jurisdiction and the due administration of the bankrupt law."

In *re Lesser Bros.*, 5 A. B. R. 320 (C. C. A. N. Y., reversed, on other grounds, sub nom. *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165): "The District Court had jurisdiction to stay the appellants by virtue of its power as a court of bankruptcy, * * * and, as § 67 gives the court of bankruptcy power to make orders in the premises, it was also proper for that court to proceed as a court of bankruptcy, by order after notice upon a summary petition, and direct the Metcalfs not to go into the State court upon their own motion and attempt to obtain payment."

§ 1474. Or May (after Adjudication) Issue Order to Surrender.—The bankruptcy court may, after adjudication of bankruptcy, issue an order upon the State Court officer to turn over the property.⁹⁷

proved in its full extent. In *re Chas. D. Adams*, 1 A. B. R. 94 (Ref. N. Y.); instance, In *re Breslauer*, 10 A. B. R. 33, 121 Fed. 910 (D. C. N. Y.); instance, where injunction refused, In *re Shoemaker*, 7 A. B. R. 437 (D. C. Va.).

As to whether referee may issue the restraining order, see ante, as to "Jurisdiction of Referees," § 527.

And the Bankruptcy Court does not lose the right to issue the restraining order in the bankruptcy proceedings themselves, by the trustee's previous application in the State Court; at any rate, where he had had no order to make the previous application.

⁹⁷. In *re Francis-Valentine Co.*, 2 A. B. R. 522, 89 Fed. 691 (C. C. A. Calif., affirming 2 A. B. R. 188); In *re Kenney*, 3 A. B. R. 353, 97 Fed. 554 (D. C. N. Y., affirmed by C. C. A., 5 A. B. R. 355, 105 Fed. 897, and by Supreme Court sub nom. *Clarke v. Larremore*, 9 A. B. R.

477, 188 U. S. 486); In *re Hoffman*, 1 A. B. R. 587 (Ref. Penn.); instance, In *re Feiser*, 7 A. B. R. 690, 115 Fed. 199 (D. C. Pa.).

Impliedly, In *re Grassler & Reichwald*, 18 A. B. R. 694, 154 Fed. 478 (C. C. A. Calif.); instance, receiver in supplementary proceedings, In *re Matthews & Sons*, 20 A. B. R. 570, 163 Fed. 127 (D. C. N. Y.); instance, constable ordered to surrender possession, In *re Cohn*, 18 A. B. R. 786 (Ref. Calif.); instance (placed however on other grounds than lien by legal proceedings), In *re Hecox*, 21 A. B. R. 314, 164 Fed. 823 (C. C. A. Colo.), quoted at § 1611.

Instance where order refused, In *re Seebold*, 5 A. B. R. 358, 105 Fed. 910 (C. C. A. La.): This case, in its last syllabus and also in the language of the opinion, seems to deny the right of the bankruptcy court to order surrender of

And it has been held that the marshal or receiver may be ordered to seize the property before adjudication;⁹⁸ but this hardly would be justified, for the lien is not annulled by the mere filing of the petition, but only by the adjudication.⁹⁹

§ 1475. **Trustee May Replevin.**—Of course, the trustee in bankruptcy may resort to replevin to gain possession.

§ 1476. **Or May Sue State Court's Officer for Money Had and Received.**—The trustee may sue the State Court's officer for money had and received; and this latter method is held in one case to be the only proper course where the property has been sold and the State court been appealed to without effect.¹ And in all these cases, of course, it is necessary for the attorney of the trustee to prove the five elements making the lien void, in order to gain possession of the property levied on.

§ 1477. **Where Sheriff Already Paid Over Proceeds to Execution Creditor Latter becomes Adverse Party Not to Be Summarily Dealt with.**—Where the sheriff has already paid over to the execution creditor the whole or a part of the proceeds of the execution sale, the execution creditor becomes an adverse party and cannot be required summarily to surrender what he has received: he can be reached only by plenary action.²

the proceeds of a levy made within four months, but it is not, perhaps, really *contra*, since the facts show the levy was simply the giving of the effect to an inchoate landlord's lien already existing and so was not within the inhibitions of § 67 (f) but rather within the doctrine of paragraph 1214, ante.

In *re Fellerath*, 2 A. B. R. 40, 95 Fed. 121 (D. C. Ohio); *contra*, In *re Franks*, 2 A. B. R. 634, 95 Fed. 635 (D. C. Ala.).

Even if a replevin proceedings is pending against the sheriff by a stranger who claims the property for himself and asserts it did not belong to the bankrupt, yet the sheriff must turn over the property to the bankruptcy trustee, since his holding of it is, in any event, without title: the stranger must work out his rights in the bankruptcy proceedings. In *re Francis-Valentine Co.*, 2 A. B. R. 522, 89 Fed. 691 (C. C. A. Calif.).

That the referee may make such order, after adjudication and reference, see ante, § 540; post, § 1827.

Contempt by officer in failing to obey order of surrender, see post, § 1856 and § 2330.

Obiter, *Staunton v. Wooden*, 24 A. B. R. 736, 179 Fed. 61 (C. C. A. Cal.). Compare post, §§ 1661, 1827.

⁹⁸. In *re Richard*, 2 A. B. R. 506 (D. C. N. Car.).

⁹⁹. Compare, ante, § 1461.

¹. In *re Franks*, 2 A. B. R. 634, 95 Fed. 635 (D. C. Ala.).

Trustee's Positive Affidavit as to Bankrupt's Insolvency.—The trustee's own positive affidavit that the bankrupt was insolvent at the time has been held sufficient proof of the element of insolvency, it not appearing that the trustee did not have the means of knowing. *Hardt v. Schuylkill Plush & Silk Co.*, 8 A. B. R. 479, 74 N. Y. Supp. 549.

². Compare, apparently *contra*, to the effect that the creditor may be ordered to surrender the proceeds of the sale of the attached property, In *re Hammond*, 3 A. B. R. 466, 98 Fed. 845 (D. C. Mass.). But obviously this was a case where the proceeds were still in the officer's hands although the Court says in the "creditors'" hands.

But if the lien by legal proceedings was obtained before the filing of the petition and within the four months, but the sale and turning over of the proceeds did not take place until after the filing of the petition and appointment of the receiver in bankruptcy although before the adjudication, the proceeds in the hands of the judgment creditor, who was cognizant of the receivership, may be summarily ordered surrendered. In *re Breslauer*, 10 A. B. R. 33, 121 Fed. 910 (D. C. N. Y.). But

Levor v. Seitor, 8 A. B. R. 459, 74 N. Y. Supp. 499: "While proceedings are pending for the enforcement of a lien created by judgment or otherwise, and before the lien is in fact satisfied by the lienor receiving the amount thereof, doubtless the trustee in bankruptcy has the right to avoid the lien or to follow the proceeds of the sale of the property to which the lien attached until they are actually paid over to the lienor. * * * Until the avails of sale actually reach the possession of the judgment creditor, the proceeding to enforce the judgment may still be regarded as incomplete; but when the proceeds are paid over, the lien of the judgment is in fact satisfied, in this case pro tanto."

In *re Blair*, 4 A. B. R. 220, 102 Fed. 987 (D. C. N. Y.): "Although the collection by execution and payment to the creditor constituted a 'preference' (§ 60a), yet as the money was received by the creditor before the petition in bankruptcy was filed, the transaction thereby became consummated, thus differing from *Kenny's case* (3 Am. B. R. 353). If the preference was received by the creditor without reasonable cause to believe a preference was intended (§ 60b), it seems not to be recoverable back by the trustee. * * *

"Under the recent decisions of the Supreme Court, I am of opinion that this transaction being completely executed by the payment of the money by the sheriff before the petition was filed, the remedy of the trustee is by plenary action alone in the State court."

Inferentially, obiter, *Clarke v. Larremore*, 9 A. B. R. 476, 188 U. S. 486: "A different question might have arisen if the writ had been fully executed by payment to the execution creditor."

In *re Knickerbocker*, 10 A. B. R. 381, 121 Fed. 1004 (D. C. N. Y.): "It is quite true that by § 67f, 30 Stat. 565, all judgments, liens, levies, and other liens are invalidated by adjudication in bankruptcy, and the property affected by them passes to the trustee; but where the proceeds of an execution sale have actually been paid to the judgment creditor—in other words, where the transaction is completely executed—the execution creditor ceases to be a lienor, but has title to the proceeds of his execution. This title may or may not be defeasible, as may be disclosed by an action brought to recover these proceeds. * * *

"The referee was of the opinion that, as the judgment was not satisfied in full by the money realized on the execution sale, the respondents were creditors of the bankrupt, and that jurisdiction may therefore be exercised over this controversy. This contention is without merit. The respondents are not now before this court in the capacity of creditors. They are not seeking to prove a claim, and no order has been made directing a surrender of a preference as a condition of its allowance. * * * The remedy of the trustee, however, must be sought in a plenary suit brought under the provisions of § 23 (b), as amended, either in this court or the proper State tribunal, at his election."

In *re Bailey*, 16 A. B. R. 289, 144 Fed. 214 (D. C. Ore.): "Being invalidated, the property is divested of the encumbrance and the trustee takes it by succession from the bankrupt as if none had ever existed or had been claimed. The distinction should be held in mind between the lien claimed on the property by virtue of the levy, attachment, etc., and the property itself. It is the lien that § 67 'f' treats of and is designed to affect directly. The property is

this would come rather under the rules relative to the superseding of receiverships.

Obiter, In *re Grassler & Reichwald*, 18 A. B. R. 694, 154 Fed. 478 (C. C. A.

Calif.); In *re Resnek*, 21 A. B. R. 740, 167 Fed. 574 (D. C. Pa.), quoted at § 1478; obiter, *Rodolf v. First Nat. Bank of Tulsa*, 28 A. B. R. 897 (Sup. Ct. Okla.).

only affected indirectly by a discharge of the lien. * * * The case at bar, however, presents a different condition from either of the foregoing, by reason of the fact that the purchaser, who is the judgment creditor, has come into the property by virtue of the sheriff's sale, which had been consummated prior to the filing of the petition in bankruptcy, and everything had been done that was required by law to be done for a transfer of the debtor's property to the purchaser, through the process of the court, so that, at the time of the filing of the petition in bankruptcy, the debtor was not the owner of the property, and not being the owner, a fortiori he was not the owner of the proceeds thereof. Keeping in mind, now, that it is the lien that is declared void by virtue of § 67f, and not the transfer, one can readily understand that the section does not affect the transaction vitally, or render it void. * * * But, while there seems to be some contradiction among the authorities as to when the summary proceeding will be entertained, it is well settled that it is not appropriate for the recovery of the property, or the proceeds thereof, after the same has passed into the hands of the purchaser, all prior to the petition and adjudication in bankruptcy. After the property has passed under such conditions, it amounts to a transfer, and it becomes a preference, if liable at all to the suit of the trustee, and the manner of recovery is prescribed by § 60a and § 60b of the Bankruptcy Act. In such events, it is also necessary to show that the preference was received by the beneficiary under a belief on his part, or having reasonable grounds therefor, that it was intended for such purpose. Otherwise, even the transfer is not voidable."

But a delivery of the attached property to the attaching creditor upon the giving of a redelivery bond by the creditor, is not within the doctrine of this paragraph, for the property, in such circumstances, is still in the custody of the court, in the eyes of the law, the bond standing in the stead of the property, in specie; and the doctrine of this paragraph refers only to the *proceeds* of property sold under order.³

§ 1478. And Recovery Only to Be Had on Other Grounds than § 67 (f).—And in case the sheriff has already paid the proceeds over to the execution creditor at the time of the filing of the bankruptcy petition, recovery can be had only on proof of a voidable preference or of some other ground of recovery than simply § 67 itself, for the proviso in § 67 (f) applies only to cases where the lien was still in existence at the time of the filing of the bankruptcy petition.⁴

Levor v. Seiter, 8 A. B. R. 459, 74 N. Y. Supp. 499, reversing S. C., 5 A. B. R. 576, 69 N. Y. Supp. 987: "If the amount were received by the creditor without reasonable cause to believe a preference was intended, it seems not to be recoverable back by the trustee.

"It is not shown in the case at bar, that the sheriff paid the money over to the judgment creditors after the petition in bankruptcy was filed. We have, there-

3. Instance, *In re Cohn*, 18 A. B. R. 786 (Ref. Calif.).

4. See ante, § 1338. Compare, obiter, *Clarke v. Larremore*, 9 A. B. R. 477, 188 U. S. 486. *In re Kenney*, 2 A. B. R. 494, 93 Fed. 427, 3 A. B. R. 353, 97 Fed. 554, 5 A. B. R. 355, 105 Fed. 897 (affirmed sub nom. *Clarke v. Larremore*, supra); *In re Bailey*, 16 A. B.

R. 289, 144 Fed. 214 (D. C. Ore.), quoted, § 1477; *In re Blair*, 4 A. B. R. 220, 102 Fed. 987 (D. C. N. Y.), quoted, § 1477; compare, to same effect, *Mohr & Sons v. Mattox*, 12 A. B. R. 330 (Sup. Ct. Ga.); compare, to same effect, *In re Sharp*, 1 A. B. R. 379 (Ref. Ky.); *In re Weitzel*, 27 A. B. R. 370, 191 Fed. 463 (D. C. N. Y.).

fore, a case which in our opinion does not fall within § 67f of the Bankrupt Law, and in which a recovery can not be had under § 60, because of the failure to prove the requirements of that section."

Botts v. Hammond, 3 A. B. R. 775, 99 Fed. 916 (C. C. A. N. Y.): "Both of these subdivisions ('c' and 'f' of § 67) deal with the lien as existing. But in the case before us the lien had been merged in the judgment; the property had been sold under lawful orders of the court, having full jurisdiction; the money has been distributed, and the lien gone. There is nothing upon which the subdivision of this section can act or to which these provisions can apply. Were it possible for the District Court, sitting in bankruptcy, to go back, and set aside every step taken, put the trustee in possession of the property, let him administer the same de novo, and pursue all the steps which have been taken, only with increased cost and expense, the petitioning creditors have lost all claim on the process of the court by their delay, after full notice, in taking any steps until the money was distributed, and all the other creditors had committed themselves and had discharged their debtor."

In *re Resnek*, 21 A. B. R. 740, 167 Fed. 574 (D. C. Pa.): "Where, within four months before the filing of a petition in bankruptcy against an insolvent debtor, an execution has been issued and levy and sale made and the proceeds paid over to the judgment creditor before the filing of the petition, the case does not fall within the provisions of § 67f of the Bankruptcy Act, and the lien created by the judgment and levy is not rendered void by the adjudication. The remedy, if any the trustee has, against the creditor, is under the provisions of §§ 60a and 60b of the Bankruptcy Act in a plenary action, where it will be necessary to allege and show that the creditor had reasonable cause to believe that the bankrupt, by suffering judgment to be taken against him, intended to give a preference."

Compare, inferentially, to same effect, *Johnson v. Anderson*, 11 A. B. R. 294 (Sup. Ct. Neb.): "In an action by a trustee in bankruptcy, to recover the proceeds of the property of the bankrupt paid over to a creditor on a judgment in completed attachment proceedings in his favor within four months before the bankruptcy, it must be alleged in the petition that the creditor had reasonable grounds to believe the bankrupt was insolvent, and that by suffering the attachment proceedings and judgment to be taken against him, thereby intending to make a preference."

Peck v. Connell, 6 A. B. R. 93 (Penn. Com. Pleas, affirmed in 8 A. B. R. 500): "If the proceedings have been allowed to go on and the lien has been enforced by sale, there is nothing which enables the money realized or the value of the property to be reached in the hands of the lien creditor. Before it had got to that point the bankrupt court might have intervened and stayed the process; or the court from which it issued, at the instance of creditors who had or were about to institute bankruptcy proceedings, might itself have done so. But the execution went on, a sale was had, and the proceeding is now closed in consequence, leaving nothing for either the bankruptcy court or this court to act upon."

And if such ground is that of preference, then reasonable cause for believing a preference would be effected must, of course, be proved; ⁵ as, for

5. *Livor v. Seiter*, 8 A. B. R. 459, 74 N. Y. Supp. 499; In *re Knickerbocker*, 10 A. B. R. 381, 121 Fed. 1004 (D. C. N. Y.); In *re Bailey*, 16 A. B. R. 289, 144 Fed. 214 (D. C. Ore.), quoted at § 1477; In *re Resnek*, 21 A. B. R. 740, 167 Fed. 574 (D. C. Pa.), quoted supra.

But perhaps if the creditor files his

claim in the bankruptcy proceedings the referee has jurisdiction to require the property seized under the void legal process to be turned over on proof of the voidability of the lien. Inferentially, In *re Huffman*, 1 A. B. R. 587 (Ref. Penn.).

instance, a preference by way of judgment "procured" or "suffered."⁶

§ 1479. Proceeds of Execution or Attachment Sale in Sheriff's Hands Pass to Trustee.—The proceeds of an execution or attachment sale still in the sheriff's hands, or in the hands of the State Court at the time of the debtor's bankruptcy, pass to the trustee, if the levy had been made within the four months while the bankrupt was insolvent.⁷

Clarke v. Larremore, Trustee, 9 A. B. R. 476, 188 U. S. 486 (affirming *In re Kenney*, 5 A. B. R. 355): "It is said that that money was not the property of the bankrupt but of the creditor in the execution. Doubtless as between the judgment creditor and debtor, and while the execution remained in force, the money could not be considered the property of the debtor, and could not be appropriated to the payment of his debts as against the rights of the judgment creditor, but it had not become the property absolutely of the creditor. The writ of execution had not been fully executed. Its command to the sheriff was to seize the property of the judgment debtor, sell it and pay the proceeds over to the creditor. The time within which that was to be done had not elapsed, and the execution was still in his hands not fully executed. The rights of the creditor were still subject to interception. Suppose, for instance, there being no bankruptcy proceedings, the judgment had been reversed by an appellate court and the mandate of reversal filed in the trial court, could it for a moment be claimed that, notwithstanding the reversal of the judgment, the money in the hands of the sheriff belonged to the judgment creditor, and could be recovered by him, or that it was the duty of the sheriff to pay it to him? The purchaser at the sheriff's sale might keep possession of the property which he had purchased, but the money received as the proceeds of such sale would undoubtedly belong and be paid over to the judgment debtor. The bankruptcy proceedings operated in the same way. They took away the foundation upon which the rights of the creditor, obtained by judgment, execution, levy and sale, rested. The duty of the sheriff to pay the money over to the judgment creditor was gone, and that money became the property of the bankrupt, and was subject to the control of his representative in bankruptcy."

Obiter, *Mohr & Sons v. Mattox*, 12 A. B. R. 332 (Sup. Ct. Ga.): "If the sheriff had immediately levied the executions and sold the property, but had not turned over the proceeds to the plaintiffs, the trustee in bankruptcy would have been entitled to the same for administration in the bankruptcy court."

6. *In re Resnek*, 21 A. B. R. 740, 167 Fed. 574 (D. C. Pa.), quoted ante.

7. *In re Richards*, 2 A. B. R. 518 (D. C. Wis., affirmed in 3 A. B. R. 145, 96 Fed. 935, C. C. A.); *In re Franks*, 2 A. B. R. 634, 95 Fed. 635 (D. C. Ala.); *Schmilovitz v. Bernstein*, 5 A. B. R. 265, 47 Atl. 884 (Sup. Ct. R. I.); *In re Kenney*, 5 A. B. R. 355, 105 Fed. 897 (C. C. A. N. Y., affirming 3 A. B. R. 353, 97 Fed. 554, and 2 A. B. R. 494 and itself affirmed sub nom. *Clarke v. Larremore*, 9 A. B. R. 477, 188 U. S. 486). *Jones v. Stevens*, 5 A. B. R. 571, 48 Atl. 170 (Sup. Jud. Ct. Mo.), in which case, however, it does not appear whether the proceeds were still in the sheriff's hands or not. Inferentially, *In re Northrop*, 1 A. B. R. 427 (Ref. N.

Y.); *In re Hammond*, 3 A. B. R. 466, 98 Fed. 845 (D. C. Mass.).

For a peculiar instance of contempt where a constable turned back to a purchaser at execution sale the excess of the proceeds of sale after satisfying a judgment for labor, but denied receipt of more than enough and failed to pay anything over to the trustee, *In re Geiser*, 12 A. B. R. 208 (D. C. Mont.).

In re Matthews & Son, 20 A. B. R. 570, 163 Fed. 127 (D. C. N. Y.); impliedly, *In re Grassler & Reichwald*, 18 A. B. R. 694, 154 Fed. 478 (C. C. A. Calif.), quoted at § 1796; impliedly, *In re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa).

Bear v. Chase, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S. C.): "But the proceeds arising from such sale must stand in lieu of the property sold, for it is expressly provided that such property shall pass to the trustee as a part of the estate, unless the lien be preserved for the benefit of the estate."

And the delivery of the attached property to the attaching creditor, under redelivery bond, would not alter the case, since such property is, in legal contemplation, still in the possession of the court's officer, the bond answering therefor.⁸

But if the levy was not made within the four months, then the mere continued possession by the sheriff of the proceeds of sale will not cause the proceeds to pass to the trustee in bankruptcy.⁹

§ 1480. Or Property Itself May Be Pursued and Recovered.—The property itself may be pursued and recovered, unless it is in the hands of a bona fide purchaser.¹⁰

Watschke v. Thompson, 7 A. B. R. 505 (Minn.): "When the trustee received his appointment * * * there was one of two courses of action open to him—to accept the result of the dissolution, and pursue the property, wherever it might be, or upon due notice, to obtain an order preserving the benefit of the attachment, if for any purpose the interests of the estate would thereby be best conserved."

§ 1481. Bona Fide Purchasers at Legal Sales Protected.—Bona fide purchasers at sales by officers of courts are protected in case subsequent bankruptcy invalidates the lien by legal proceedings.¹¹

8. Compare, ante, § 1477. Instance, *In re Cohn*, 18 A. B. R. 786 (Ref. Calif.).

9. *In re Easley*, 1 A. B. R. 715, 93 Fed. 419 (D. C. Va.). But see as to right of bankruptcy court to order summary delivery of the property subject to the lien of the levy, post, § 1816.

10. Bankr. Act, § 67 (f); *In re Breslauer*, 10 A. B. R. 33, 121 Fed. 910 (D. C. N. Y.).

Compare facts [sold subsequent to adjudication in another State], *Staunton v. Wooden*, 24 A. B. R. 736, 179 Fed. 61 (C. C. A. Cal.).

11. Bankr. Act, § 67 (f): "Provided that nothing herein contained shall have the effect to destroy or impair the title obtained by such levy, judgment, attachment or other lien, of a bona fide purchaser for value who shall have acquired the same without notice or reasonable cause for inquiry."

Inferentially, obiter, *Jones v. Stevens*, 5 A. B. R. 571, 94 Me. 582 (Sup. Jud. Ct. Me.); obiter, *In re Kenney*, 2 A. B. R. 494 (D. C. N. Y.), and 3 A. B. R. 353, affirmed by 5 A. B. R. 355, 105 Fed. 897.

Instances where held not bona fide purchasers without notice, etc.: 1. Son purchasing \$500 of property at attach-

ment sale of his father's goods for \$50, where the sale was made the day after the petition in bankruptcy was filed against the father, was held not within the protection of the proviso, *In re Goldberg*, 10 A. B. R. 97 (D. C. N. Y., Ray, J.). Also, same case in 9 A. B. R. 156, 117 Fed. 692.

2. Purchaser at execution sale: assignee's attorney present, forbidding sale and flourishing a copy of the debtor's general assignment; debtor himself present proclaiming his own insolvency; thereafter bankruptcy; held, purchaser not a purchaser without notice nor reasonable cause for inquiry, *Brown v. Case*, 6 A. B. R. 744, 61 N. E. 279, 180 Mass. 45.

3. Attaching creditor not purchaser for value in good faith under the bankruptcy act, notwithstanding statutory provisions of the State, *In re Kaupisch Creamery Co.*, 5 A. B. R. 790, 107 Fed. 93 (D. C. Ore.).

4. Purchaser at execution sale after filing of petition but before adjudication, *In re Breslauer*, 10 A. B. R. 33, 121 Fed. 910 (D. C. N. Y.).

5. Purchaser buying only "the bankrupt's interest" and being notified of attachments levied more than four

Clarke v. Larremore, 9 A. B. R. 478, 188 U. S. 486: "It is true that the stock and fixtures, the property originally belonging to the bankrupt, had been sold, but having, so far as the record shows, passed to a 'bona fide purchaser for value,' it remained by virtue of the last clause of the section the property of the purchaser, unaffected by the bankruptcy proceedings."

In *re Franks*, 2 A. B. R. 634, 95 Fed. 635 (D. C. Ala.): "The property, however, has passed into the hands of a third person under a sale by the sheriff, and it may be assumed that such person is a bona fide purchaser for value, and that the trustee cannot for that reason recover and reclaim it from him. But whether this be so or not, the trustee has an equal right to claim and recover the proceeds of the sale."

§ 1482. Purchaser Has Burden of Proof of Bona Fides.—The purchaser at a judicial sale has the burden of proof that he is within the proviso of § 67 (f).¹²

§ 1483. Sheriff Paying Over Proceeds before Filing of Petition Protected.—If the sheriff or other officer pays over the proceeds of the sale under the judicial process that was levied within the four months preceding the filing he may not be sued therefor, at any rate if he pays them over before the filing of the petition.¹³

§ 1484. But Perhaps Liable if Pays after Petition Filed.—But if he pays them over after the filing of the bankruptcy petition, probably he is liable therefor.¹⁴

And the trustee and creditors can hardly be charged with laches, because the lien is absolutely null and void.¹⁵

§ 1484½. If Pays after Bankruptcy, Creditor Summarily Ordered to Surrender.—If the sheriff pay over the proceeds to the creditor after the bankruptcy, the creditor may be ordered summarily to surrender them.¹⁶

In *re Grassler & Reichwald*, 18 A. B. R. 694, 154 Fed. 478 (C. C. A. Calif.): "If the property had been in the adverse possession of the petitioner before the bankrupts filed their petition to be adjudicated bankrupts there can be no doubt that a plenary suit would have been necessary. But assuming, as we may under the record, the facts to have been, as it is claimed by the respondent herein that they were, that certain property of the bankrupts was taken

months prior to the bankruptcy, *Batchelder v. Wedge*, 19 A. B. R. 268, 80 Vt. 353.

In *re Weitzel*, 27 A. B. R. 370, 191 Fed. 463 (D. C. N. Y.). Compare [where sale not made until after adjudication, though made in another state than that where the bankruptcy proceedings were pending], *Staunton v. Wooden*, 24 A. B. R. 736, 179 Fed. 61 (C. C. A. Calif.).

12. *Mencke v. Rosenberg*, 9 A. B. R. 323, 202 Penn. St. 131.

Injunction may issue to restrain proceedings until the question of setting aside the sale may be decided, In *re*

Goldberg, 9 A. B. R. 156, 117 Fed. 692 (D. C. N. Y.).

13. But compare, perhaps contra, *Jones v. Stevens*, 5 A. B. R. 571, 48 Atl. 170, 94 Me. 582.

14. Compare, In *re Richard*, 2 A. B. R. 506 (D. C. N. Car.); compare, In *re Breslauer*, 10 A. B. R. 33, 121 Fed. 910 (D. C. N. Y.).

15. *Hardt v. Schuylkill Plush & Silk Co.*, 8 A. B. R. 479 (Sup. Ct. N. Y. App. Div.).

16. Obiter and impliedly [not proceeds but property itself pursued], *Staunton v. Wooden*, 24 A. B. R. 739, 179 Fed. 61 (C. C. A. Cal.).

upon a void attachment and that the money realized on the sale thereof was paid to the petitioner on a judgment entered in his favor by default against the bankrupts several weeks after they had filed their petition in the District Court to be adjudicated bankrupts, and that this was known to the petitioner, we think there can be no question that under the provisions of § 2 (7) and § 67f of the Bankruptcy Act, authorizing the referee to compel the surrender of funds to the trustee, the proceeding had before the referee in this case was permissible."

And where several creditors receive different portions of the proceeds from the sheriff, under a common scheme to thwart the creditors in bankruptcy, an order against them all jointly will lie.¹⁷

§ 1485. Lien for Costs Falls with the Rest.—The lien for the plaintiff's costs falls with the execution or attachment lien itself and the sheriff has no right to retain his fees out of the property turned over, nor are the costs entitled to priority of payment out of the bankrupt estate,¹⁸ unless the lien is preserved for the benefit of the estate.

In *re Allen*, 3 A. B. R. 38, 96 Fed. 912 (D. C. Calif.): "It is true that, under the laws of the State of California, the Sullivan-Kelley Company acquired a lien upon the property attached in its suit against the bankrupt for the satisfaction of any judgment which it might recover in that action, and which judgment would of course, include the costs of the action; but this lien was dissolved by the adjudication in bankruptcy (Subdivisions c, f, § 67. *Id.*; In *re Ward*, 9 N.

¹⁷. *Ryan v. Hendricks*, 21 A. B. R. 570, 166 Fed. 94 (C. C. A. Wis.).

¹⁸. In *re Jennings*, 8 A. B. R. 358 (Ref. N. Y.); In *re Beaver Coal Co.*, 5 A. B. R. 787, 107 Fed. 98; also, 6 A. B. R. 404, 107 Fed. (D. C. Ore.), affirmed in 7 A. B. R. 542; In *re Iroquois Mach. Co.*, 22 A. B. R. 183, 166 Fed. 629 (D. C. R. I.), quoted at § 2197. But compare, In *re Schmidt & Co.*, 21 A. B. R. 593, 165 Fed. 1006 (C. C. A. N. Y.), quoted at § 1486; In *re Goldberg Bros.*, 16 A. B. R. 521, 144 Fed. 566 (D. C. Me.); apparently contra, In *re Copper King*, 16 A. B. R. 149, 144 Fed. 689 (D. C. Calif.). See post, §§ 1618, 1619.

In *re The Copper King*, 16 A. B. R. 149, 144 Fed. 689 (D. C. Calif.); In *re Young*, 2 A. B. R. 673, 96 Fed. 606 (D. C. N. Y.); In *re Thompson Mercantile Co.*, 11 A. B. R. 579 (Ref. Minn.); (1867) In *re Fortune*, 2 B. Reg. 662; (1867) *Gardner v. Cook*, 7 B. Reg. 346; (1867) In *re Ward*, 9 B. Reg. 349; (1867) In *re Hatje*, 12 B. Reg. 548; (1867) In *re Preston*, 6 B. Reg. 545. (1867) But contra, apparently, In *re Foster*, 2 Story 131; (1867) In *re Housberger*, 2 Ben. 504, 2 B. Reg. 92; (Eng.) *London v. King*, 50 Geo. 302.

In *re Francis-Valentine Co.*, 2 A. B. R. 522 (Affirming 2 A. B. R. 188, 93 Fed. 935, D. C. Calif.): In the case

in the District Court, the court did not decide whether the lien itself was void but merely that the sheriff must turn over all the proceeds and work out his lien, if he had any, in the bankruptcy court.

And it is perhaps to be inferred from one case that the sheriff or other court officer may be entitled to his costs as an equitable lien, like assignees on turning over assigned property in case perhaps the attachment operated to benefit all creditors. In *re Francis-Valentine Co.*, 2 A. B. R. 522 (affirming 2 A. B. R. 188, 93 Fed. 945, D. C. Calif.). Such right, however, could not be deemed a right of "priority" for the "actual and necessary expense of preserving the estate" under § 64 (b) except perhaps as to such part thereof as accrued "subsequent to the filing of the petition;" nor could it come within the other priority accorded by § 64 (b) (2) unless it operated to "recover property fraudulently transferred or concealed," which an attachment could hardly be said to accomplish. Compare, to such effect, under the law of 1867, In *re Fortune*, 2 B. Reg. 662; *Gardner v. Cook*, 7 B. Reg. 346; In *re Ward*, 9 B. Reg. 349; In *re Jenks*, 15 B. Reg. 301; *Zeiber v. Hill*, 8 B. Reg. 239; In *re Holmes*, 14 B. Reg. 493.

B. R. 349, Fed. Cas. No. 17145), leaving to that company only the right to prove the debt sued for, and the costs incurred in good faith prior to the filing of the petition in bankruptcy, as an unsecured claim against the estate of the bankrupt."

But, in cases where State or United States laws give priority to the costs, they may have the same priority in bankruptcy, under § 64 (b) (5).¹⁹

In *re Lewis*, 4 A. B. R. 51, 99 Fed. 935 (D. C. Mass.): "Priority of a sheriff's (attachment) fees under the Massachusetts statute (insolvency) will be recognized and enforced in the bankruptcy court by virtue of § 64 (b) (5) giving priority to debts owing to any person who by the laws of the State or the United States is entitled to priority."

§ 1486. Sheriff No Right to Retain Creditor's Costs, nor to Retain Property Till Costs Paid.—At any rate, the sheriff has no right to retain the execution creditor's costs out of the proceeds of sale nor to retain the property until the costs are paid, for those costs are a claim only against the one who made them, namely, the creditor himself, and are not a lien on the fund; since the creditor himself has no valid lien therefor.²⁰

But compare, In *re Schmidt & Co.*, 21 A. B. R. 593, 177 Fed. 1006 (C. C. A. N. Y.), which arose upon a petition to review an order directing the trustee in bankruptcy to pay the fees of the sheriff of New York on two executions levied upon property of the bankrupt within four months prior to the filing of the petition in bankruptcy. "We are satisfied that the language used by Congress in the 67th section of the Bankrupt Act providing that levies under judgment within the period named 'shall be deemed null and void' was not intended to deprive the State's officer of his statutory fees, accruing prior to bankruptcy, under proceedings in the State courts, which were in all respects regular and in accordance with the State law and practice."

However, it may be proper for the sheriff to retain out of the fund in his hands the costs which the bankrupt himself made.

§ 1487. Creditor May Prove Claim Where Lien Nullified, Also Costs.—The creditor whose lien is thus rendered null and void by the bankruptcy is not debarred from proving his claim as an unsecured debt for sharing in the dividends.²¹ And he may also prove his costs.²²

And if the attachment does not fall, neither does the sheriff's lien for costs. In *re Beaver Coal Co.*, 7 A. B. R. 542 (C. C. A. Ore., affirming 6 A. B. R. 404, 110 Fed. 630).

19. Complete discussion and citation of cases, see post, §§ 2196, 2197.

20. In *re Francis-Valentine Co.*, 2 A. B. R. 522, affirming 2 A. B. R. 188, 93 Fed. 935 (D. C. Calif.); (1867) In *re Ward*, 9 B. Reg. 349; (1867) *Zeiber v. Hill*, 8 B. Reg. 239; (1867) In *re Stevens*, 5 B. Reg. 298; (1867) *Hannon v. Jamieson*, 1 Cranch C. C. 288. (Eng.). Compare, however, *London v. King*, 50 Geo. 302; (1867) In *re Fortune*, 1 Low 306; In *re Foster*, 2 Story

131; (1867); In *re Preston*, 5 B. Reg. 293 and 6 B. Reg. 545; (1867) In *re Housberger*, 2 B. Reg. 92; (1867) In *re Jenks*, 15 B. Reg. 301; (1867) In *re Holmes*, 14 B. Reg. 493; (1867) *Gardner v. Cook*, 7 B. Reg. 346.

21. In *re Gerson Richard*, 2 A. B. R. 506, 94 Fed. 633 (D. C. N. Car.); impliedly, In *re Richard T. Richards*, 2 A. B. R. 518 (D. C. Wis.); In *re Allen*, 3 A. B. R. 39, 95 Fed. 512 (D. C. Calif.).

22. In *re Allen*, 3 A. B. R. 38, 95 Fed. 512 (D. C. Calif.); In *re Thompson Mercantile Co.*, 11 A. B. R. 579 (Ref. Minn.). [1867] *Contra*, In *re Ward*, 9 B. Reg. 349. [1867] *Contra*, *Zeiber v. Hill*, 8 B. Reg. 239.

§ 1488. Creditor Whose Lien Nullified under No Duty to Keep Officer in Possession.—The creditor whose lien is thus dissolved is under no duty to keep the sheriff or other officer in possession, but may turn the property back to the bankrupt, if no receiver or trustee has been appointed;²³ if, however, he does retain possession, the bankruptcy court is to determine for itself what is the reasonable expense of the preservation, and is not bound by the amount actually paid for keeper's fees;²⁴ nor by the sheriff's statutory costs.

§ 1488½. Seizure from Sheriff by Third Person.—After adjudication the possession of the sheriff or other levying officer where the lien is thus nullified under § 67 is not adverse to the bankruptcy court.²⁵

And a seizure, by replevin or otherwise, from his custody, has been treated as a direct interference with the custody of the bankruptcy court.

In re Walsh Bros., 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa): "It is urged that, if the plaintiffs in the several replevin suits sold the property replevied by them respectively to the bankrupts, under such circumstances as will entitle them to rescind the sales and reclaim the property, the title to such property would not pass to the trustee in bankruptcy. The merits of this contention will not be heard or considered upon this hearing. It is admitted that the property had been delivered to the bankrupts pursuant to contracts of purchase thereof, and was in their possession when it was seized by the sheriff under the attachment, and was in his custody at the time of the adjudication in bankruptcy. The adjudication in bankruptcy discharged the attachment and released the attached property therefrom, unless the court of bankruptcy shall order the lien preserved for the benefit of the bankrupt estate. Bankruptcy Act, § 67f, * * * The adjudication also operated as a seizure of the property, and it was in custodia legis from that time; and upon the appointment and qualification of the trustee the title and right thereto passed to the trustee, who then became its legal custodian for the court of bankruptcy, and that court will award it to whomever it rightly belongs. White v. Schloerb, 178 U. S. 542, 4 Am. B. R. 178, * * * In re Granite City Bank, 14 Am. B. R. 404, 137 Fed. 818, * * * The seizure of the property upon the writs of replevin was therefore a direct interference with the rightful custody of the court of bankruptcy and wholly unauthorized. White v. Schloerb, 178 U. S. 542, 4 Am. B. R. 178."

And such seizure has been held to be a contempt of the bankruptcy court.²⁶

§ 1489. Preservation of Lien for Benefit of Estate.—The court may, on due notice, order that the right under such levy, judgment,

²³ In re Allen, 3 A. B. R. 38, 96 Fed. 912 (D. C. Calif.).

For case of subrogation to lien of nullified attachment, see In re Hammond, 3 A. B. R. 491, 98 Fed. 845 (D. C. Mass.).

For case of allowing suit to proceed to enable creditor to obtain lien on exempt property; In re Jackson, 8 A. B. R. 594 (D. C. Penn.).

No costs against successful re-

claimer, In re Neely, 7 A. B. R. 312, 113 Fed. 210 (C. C. A. N. Y.).

²⁴ In re Allen, 3 A. B. R. 38, 96 Fed. 912 (D. C. Calif.).

²⁵ In re Walsh Bros., 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa), quoted further at § 1897. Also see § 1661.

²⁶ In re Walsh Bros., 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa), quoted further at § 1807.

attachment or other lien be preserved for the benefit of the estate, and thereupon the same may pass to and be preserved by the trustee for the benefit of the estate, although void as to the particular creditor so levying.²⁷

First Nat'l Bk. *v.* Staake, 15 A. B. R. 642, 202 U. S. 141: "This section (67f) makes two distinct provisions for the disposition of the property of an insolvent attached within four months prior to the filing of a petition in bankruptcy against him. First, such attachments shall be declared null and void, and the property affected shall be deemed released, and shall pass to the trustee of the estate of the bankrupt; or second, the court may order that the right acquired by the attachment shall be preserved for the benefit of the estate. In the first case the whole property passes free from the attachment. In the second, so much of the value of the property attached as is represented by the attachments passes to the trustee for the benefit of the entire body of creditors that is 'for the benefit of the estate'—in other words the statute recognizes the lien of the attachment, but distributes the lien among the whole body of creditors.

"The first provision contemplates the attachment of property to which the bankrupt has the complete legal and equitable title, which, as soon as the attachment is dissolved, passes at once to the bankrupt's trustee as part of his estate. The second provision evidently does not apply to this, as there is no object in preserving the lien of the attachment for the benefit of the estate, since under the first clause the entire value of the property attached passes to the trustee free from the attachment. The second clause contemplates property in which the bankrupt has an interest which has been secured to attaching

27. Bankr. Act, § 67 (f): "Unless the court shall, on due notice, order that the right under such levy, judgment, attachment, or other lien shall be preserved for the benefit of the estate; and thereupon the same may pass to and shall be preserved by the trustee for the benefit of the estate as aforesaid."

Also, Bankr. Act, § 67 (b): "Whenever a creditor is prevented from enforcing his rights as against a lien created by his debtor, who afterwards becomes a bankrupt, the trustee of the estate of such bankrupt shall be subrogated to and may enforce such rights of such creditor for the benefit of the estate."

Instance, *Martin v. Globe, etc., Co.*, 27 A. B. R. 545, 193 Fed. 841 (C. C. A. Ky.); *Obiter*, impliedly, *In re Hinsdale*, 7 A. B. R. 85, 111 Fed. 502 (D. C. Vt.); *In re Lesser*, 5 A. B. R. 326 (C. C. A., affirming 3 A. B. R. 815, but itself reversed sub nom. *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165; *Patten v. Carley*, 8 A. B. R. 482 (N. Y. Sup. Ct. App. Div.); *Thompson v. Fairbanks*, 13 A. B. R. 446, 196 U. S. 516; impliedly, *In re Howland*, 6 A. B. R. 495 (Ref. N. Y.); *In re Merrow*, 12 A. B. R. 615, 131 Fed. 993 (D. C. Mass.); *In re Kenney*, 5 A. B. R. 355, 105 Fed. 897 (C. C. A. N. Y., affirming

3 A. B. R. 353, and 2 A. B. R. 494 and itself affirmed sub nom. *Clarke v. Larremore*, 9 A. B. R. 476, 188 U. S. 486); *In re Adams*, 1 A. B. R. 94 (Ref. N. Y.); *Obiter*, impliedly, *In re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa); *Good-nough Stock Co. v. Galloway*, 22 A. B. R. 803, 171 Fed. 940 (D. C. Ga.); *obiter*, impliedly, *Davis v. Crompton*, 20 A. B. R. 53, 158 Fed. 735 (C. C. A. Pa.), quoted at § 1243¼; *Conti v. Sunseri*, 18 A. B. R. 891 (Pa. Com. Pleas).

Instance, *In re S. Ah. Mi.*, 18 A. B. R. 138 (D. C. Hawaii); *Indirect Order of Preservation*: "Judgment was obtained by a creditor against the bankrupt more than four months previous to adjudication, and execution taken out and levy made within the four months. Sale of the property had been advertised and was about to be made, at the date of adjudication. On motion of plaintiff and for saving of expense to the estate, the court of bankruptcy ordered the officer making the levy to proceed with the sale."

Compare, where nullification of lien or supersedeence of State court's custody occurs through § 67 (c) rather than § 67 f., *First Nat. Bk. v. Title & Trust Co.*, 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.), quoted at §§ 1446, 1491, 1603.

creditors by the levy of the writ, but which might have passed to another person, as, for instance, a purchaser under an unrecorded deed, but for the fact that the attaching creditors had acquired a prior lien thereon. In such case the statute recognizes the validity of the lien, but preserves it for the benefit of the entire body of creditors, by reason of the fact that the attachment was dissolved as a preferential lien in favor of the attaching creditors, by the institution of proceedings in bankruptcy.

"In the present case Baird had contracted to convey the property to the Roanoke Furnace Company, possession had been taken and the consideration paid, but the deed was not actually executed and recorded until after the attachment had been levied. Hence, under the Virginia statute, the validity of which is not questioned, the lien of the attachment took precedence of the deed, and would have remained a prior lien, had it not been for the institution of the bankruptcy proceedings within four months. This dissolved the attachment, and had the case rested here, the property would have apparently passed to the Furnace Company, or to its trustee in bankruptcy, Shimer; but at this point the court, under the second proviso of 67f, interposed and recognized the lien of the attachment, not, however, solely for the benefit of the attaching creditors, but for the benefit of Baird's estate. Shimer made no objection, and the court declined to express an opinion as to his rights.

"This is one of the very contingencies provided for by the second clause of the section, which apparently vests in the court a certain discretion with regard to the preservation of the right acquired under the attachment or other lien. In this case the court recognized the validity of the lien, the trustee of the Furnace Company making no objection to this; but the attaching creditors insist that, as the lien was acquired for their own benefit, they should not be required to share with the general creditors of Baird's estate."

In *re New York Economical Printing Co.*, 6 A. B. R. 615, 110 Fed. 518 (C. C. A. N. Y.): "Subdivision 'b' § 67 (Act of 1898), preserves for the benefit of the estate in bankruptcy a right which some particular creditor has been prevented from enforcing by the intervention of the debtor's bankruptcy. If a creditor, by an execution or a creditors' bill, has secured a legal or equitable lien upon the mortgaged property before the mortgagor has been adjudicated a bankrupt, under this provision his rights will or will not inure to the benefit of the estate, depending upon the time when the lien was acquired. If acquired more than four months before the commencement of the bankruptcy proceeding, his lien would inure to his own exclusive benefit; but, if acquired at any time within the four months, it would be null and void, under subdivision 'f' of the section, except as preserved for the benefit of the estate as provided in that subdivision and in subdivision 'b.'"

In *re Baird*, 11 A. B. R. 438, 126 Fed. 845 (D. C. Va.): "The power of the court, and indeed its duty to take away from the attaching creditors the benefit of their liens and give it to the trustee is found specifically in § 67f."

Obiter, *Watschke v. Thompson*, 7 A. B. R. 504 (Sup. Ct. Minn.): "The adjudication in bankruptcy had the effect of dissolving the attachment against the property of the bankrupt and restoring the title of the property to the estate. When the trustee received his appointment, on Nov. 29th, there was one or two courses of action open to him; to accept the result of the dissolution, and pursue the property, wherever it might be, or, upon due notice, to obtain an order preserving the benefit of the attachment, if for any purpose the interests of the estate would thereby be best conserved."

Obiter, In *re Sentenne & Green Co.*, 9 A. B. R. 648, 120 Fed. 436 (D. C. Pa.): In this case the question arose as to whether certain after-acquired property came under the lien of a chattel mortgage attempting to cover after-acquired

property and if so, whether attachments cut off the mortgagee's right as to such property and should be preserved for the benefit of the creditors in bankruptcy, the court finally refusing to order preservation because of inequity, saying, however, obiter, "But it is conceded that, *In re New York Economical Printing Co.*, 6 Am. B. R. 615, 49 C. C. A. 133, 110 Fed. 514, the Circuit Court of Appeals of this circuit determined that a trustee was not permitted to attack the mortgage unless he represented a creditor 'armed with process;' but the trustee urges that he is thus enabled by the fact that he has been subrogated by the order of this court to the rights of the creditors who levied attachments upon the after-acquired property, even before there was any attempt to foreclose the mortgage. If the order of subrogation be allowed to stand, the trustee's position seems to be correct."

The levying creditor derives no special benefit from the preserving of the lien. It is not preserved for his benefit. Thus the trustee is obliged to assume two apparently inconsistent attitudes—in the State Court, that the lien is valid, in the bankruptcy court, that it is void. These attitudes are really not inconsistent, however, for the lien is valid in the State Court and invalid in the bankruptcy court.

Subrogation to nullified attachment liens, which under State law would have cut off chattel mortgagees' rights to after-acquired property, has been sometimes granted²⁸ and sometimes refused²⁹ on grounds of equity.

Likewise, the preservation of other attachment liens, which would have cut off intervening rights, have been granted³⁰ or refused as the court has deemed equitable.

Likewise, subrogation to the nullified liens of creditors' bills has been sometimes granted,³¹ and at other times refused³² as the court has deemed equitable.

The lien of an assignment for the benefit of creditors has been preserved in order to invalidate unrecorded liens which otherwise would be good as against the trustee in bankruptcy.

In re Fish Bros. Wagon Co., 21 A. B. R. 149, 164 Fed. 553 (C. C. A. Kans.): "We think that a title or lien acquired by an assignee under a general assignment valid according to the law of the State where it is made, that is to the advantage of the estate when it has passed into bankruptcy, is not necessarily destroyed by the supersession of the assignment proceeding, but that upon the order of the court of bankruptcy it may be retained by the trustee for the benefit of the creditors. This conclusion is in harmony with the object sought by express provisions of the Bankruptcy Act for the preservation of liens obtained in judicial proceedings against the debtor, and it is a fair corollary of the settled rule allowing the assignee compensation for acts that are beneficial to the estate which afterwards passes to the trustee."

28. *In re New England Piano Co.*, 9 A. B. R. 763, 122 Fed. 937 (C. C. A. Mass.).

29. *Thompson v. Fairbanks*, 13 A. B. R. 437, 196 U. S. 516; *In re Moore*, 6 A. B. R. 175, 107 Fed. 234 (D. C. Vt.); *In re Sentenne & Green Co.*, 9 A. B. R. 648, 120 Fed. 436 (D. C. Penn.).

30. *Receivers v. Staake*, 13 A. B. R.

281, 133 Fed. 717 (C. C. A. Va.); *In re Merrow*, 12 A. B. R. 615, 131 Fed. 993 (D. C. Mass.).

31. *Patten v. Colley*, 8 A. B. R. 482 (N. Y. Sup. Ct. App. Div.), Apparently, *Dunn Salmon Co. v. Pillmore*, 19 A. B. R. 172 (N. Y.).

32. *Kohout v. Chaloupka*, 11 A. B. R. 265 (Sup. Ct. Neb.).

Similarly, the liens of executions have been preserved, to cut off unrecorded conditional sales contracts and other unrecorded instruments.

Plow Co. v. Reardon, 222 U. S. 354, 27 A. B. R. 492 (affirming *Reardon v. Plow Co.*, 22 A. B. R. 26, 168 Fed. 654 C. C. A.): "The claim of the trustee was in substance (1) that delivery to the sheriff of executions upon the Sechler and Cordage judgments operated without levy to create liens upon the real and personal property of Brown, the judgment debtor, within the county; (2) that such liens were paramount to rights in the property possessed by a vendor under a contract of conditional sale; and (3) that the effect of the subrogation order was to render inoperative as a preference the liens obtained by the judgment creditors through their executions, and to preserve such liens as of the date of the filing of the proceedings in voluntary bankruptcy for the benefit of the estate in bankruptcy. That the Circuit Court of Appeals rightly held the affirmative of these three propositions we entertain no doubt. Upon the first two propositions that court said:

"As the law of Illinois must govern the answer to both questions, and the rule there is well settled, as we believe, for an affirmative answer to each, no difficulty appears in the solution. Paragraph 9 of chapter 77, Rev. Stat. 1874 (2 Starr & C. Anno. Stat. 1896, p. 2336) provides: "No execution shall bind the goods and chattels of the person against whom it is issued until it is delivered to the sheriff or other proper officer to be executed." This is a modification of the rule at common law which created a lien from the issuance of the writ, and its effect to create a lien in favor of the execution creditor is recognized in numerous decisions noted in Starr & C. Anno. Stat. supra. See *Frink v. Pratt*, 130 Ill. 327, 331, 22 N. E. 819, one of the citations in appellee's brief. The cases cited contra. declaratory of the rule that an officer receiving the execution has "no interest in the property itself" to maintain an action therefor "until after a levy," do not touch the present inquiry of lien in favor of the execution creditor, and are plainly inapplicable. Upon the second question, it is stated in *Gilbert v. National Cash Register Co.*, 176 Ill. 288, 296, 52 N. E. 22, that "whatever may be the rule in other jurisdictions," this rule is established in Illinois: "If a person agrees to sell to another a chattel on condition that the price shall be paid within a certain time, retaining the title in himself in the meantime, and delivers the chattel to the vendee so as to clothe him with an apparent ownership, a bona fide purchaser or execution creditor of the latter is entitled to protection as against the claim of the original vendor." The authorities there cited for such rule are deemed sufficient reference; and we remark that no departure appears from the doctrine thus stated in any of the Illinois cases called to our attention.'

"As the execution issued upon the judgments, which executions were held under conditional sale contracts, and such liens were paramount to the rights of the vendor, the plow company, it is manifest that the right of the judgment creditors to resort to such property in satisfaction of their liens could not be destroyed by a mere transfer of possession from one party to the contract to the other party thereto. It also follows in reason, we think, that the liens of the execution creditors in the property as they existed when the petition in voluntary bankruptcy was filed could not be subsequently destroyed by the acts of the creditors, the third parties, to the prejudice of the estate, and that if the rights of the bankrupt estate could be lost by the laches of the trustee, the record presents no evidence of such laches."

Reardon v. Rock Island Plow Co., 22 A. B. R. 26, 168 Fed. 654 (C. C. A. Ills.): "The Bankruptcy Act provides (§ 67b, c. f.) for the preservation of liens in favor of the estate, when obtained by any creditor of the bankrupt, through legal proceedings or otherwise, and set aside in bankruptcy, with the

trustee subrogated therein for their enforcement; and the effect of this provision, in reference to an order in bankruptcy so preserving a lien obtained in legal proceedings, is not open to question (*First National Bank v. Staake*, 202 U. S. 141, 146, 148, 15 Am. B. R. 639, 26 Sup. Ct. 580, 50 L. Ed. 967) as rendering it inoperative as a preference, while the statute recognizes its force otherwise, but 'distributes the lien among the whole body of the creditors,' in conformity with the policy of the act. The executions described in the bill were issued in favor of judgment creditors of the bankrupt and in the hands of the sheriff for levy; and when bankruptcy intervened, liens being claimed, the court made this statutory order, on notice to the claimants—the only notice, as we believe, intended by the provision—so that the trustee became subrogated to any lien obtained by such creditors, as of the date of the adjudication of bankruptcy."

Likewise, the lien of creditors under a suit to set aside a transfer that is preferential under State law but not under the Bankruptcy Law has been preserved.

Miller v. Acid & Fertilizer Co., 21 A. B. R. 416, 211 U. S. 496 (affirming 117 La. 821): "It is obvious that if, at the time of the alleged preferential transfer to Miller, there were no other creditors of the individual estate of Guillory than Miller, under the rule laid down by the Bankrupt Act, the transfer to him of assets of the individual estate, in payment of an individual debt, did not constitute a preference. That it might have constituted a preference under the State law results from the difference in the classification made by the State law, on the one hand, and the bankruptcy law on the other. * * * As the suit by the creditors was brought within four months before the adjudication in bankruptcy, [the filing of the petition?] their right to a lien or preference arising from the suit was annulled by the provisions of subdivision f of § 67 of the bankrupt law. But that section authorized the trustee, with the authority of the court, upon due notice, to preserve liens arising from pending suits for the benefit of the bankrupt estate, and to prosecute the suits to the end for the accomplishment of that purpose. * * * It is inferable that the parties proceeded." [For further quotation, see § 1491.]

Of course orders of subrogation are improper where the lien by legal proceedings was obtained more than four months before the filing of the bankruptcy petition.³³

No order of subrogation will be granted where the lien is upon property not exempt as to the lien but exempt as to others.

In *re Jackson*, 8 A. B. R. 594 (D. C. Pa.): "The referee refused to make the order holding that exempt property could not be administered by a court of bankruptcy and that the effect of the order prayed for would be to draw the administration of such property into this court. I agree with him."

The referee has jurisdiction to order the trustee to intervene.³⁴

§ 1490. Costs of Court Remain Lien in Cases of Preservation.—Costs of Court in cases where liens are thus preserved for the benefit of the

³³. *Nat'l Bk. v. Moses*, 11 A. B. R. 772 (Sup. Ct. N. Y.).

³⁴. *Conti v. Sunseri*, 18 A. B. R. 891 (Pa. Com. Pleas.).

estate probably would not fall, but would be a lien on the fund as it comes into the bankruptcy court.³⁵

§ 1491. Order of Preservation Requisite.—The bankruptcy court must enter some order to the effect that the lien is preserved for the benefit of the estate, otherwise it is not preserved.³⁶

In re Baird, 11 A. B. R. 438, 126 Fed. 845 (D. C. Va.): "It is further argued that the case at bar is not within the intent of the Act, because the right here contended for by the trustee is not mentioned in § 70 (a) of the Act. This argument does not seem to me to be of any force. Section 70 (a) is an enumeration of those properties the title to which passes to the trustee by operation of law. The right here asked for by the trustee can be given him only by order of court. It would have been inconsistent, even absurd, to have provided in § 70 (a) that the rights of attaching creditors in a case such as we have here shall vest in the trustee by operation of law, when it had been provided in 67 (f) that such rights should be vested in the trustee by order of court."

Watschke v. Thompson, 7 A. B. R. 504 (Sup. Ct. Minn.): "Such an action cannot be maintained unless it is based upon the order of the court provided for in subdivision 'f' of § 67, preserving the attachment for the benefit of the estate."

Thompson v. Fairbanks, 13 A. B. R. 437, 196 U. S. 516: "The mortgage assigned to the bank, and the attachment obtained by Ryan, having been dissolved by the bankrupt proceedings, the defendant's rights under his mortgage of April 15, 1891, stood the same as though there had been no subsequent mortgage given, or attachment levied. This is the view taken by the State court of the effect of the dissolution of the mortgage and attachment liens under the Bankrupt Act, and we think it is a correct one. It is stated in the opinion of the State court as follows:

"It is urged that with the annulment of the attachment, the property affected by it passed to the trustee as a part of the estate of the bankrupt under the express provisions of § 67f. There would be more force in this contention were it not for the provision that, by order of the court, an attachment lien may be preserved for the benefit of the estate. If there is no other lien on the property, there can be no occasion for such order; for, on the dissolution of the attachment, the property, unless exempt, would pass to the trustee anyway. It is only when the property for some reason may not otherwise pass to the trustee as a part of the estate that such order is necessary. We think such is the purpose of that provision, and that unless the lien is preserved, the property, as in the case at bar, may be held upon some other lien, and not pass to the trustee. Re Sentenne & G. Co., 9 A. B. R. 648, 120 Fed. 436."

35. Obiters, In re Thompson Mercantile Co., 11 A. B. R. 579 (Ref. Minn.); inferentially, In re Goldberg Bros., 16 A. B. R. 522, 144 Fed. 566 (D. C. Me.); Receivers v. Staake, 13 A. B. R. 281, 133 Fed. 717 (C. C. A. Va.). See ante, § 693.

36. Obiters and impliedly, In re Hinsdale, 7 A. B. R. 85, 111 Fed. 502 (D. C. Vt.): "The property had been attached before the bankruptcy proceedings, but, if that attachment became a lien paramount, it could probably be preserved only by the trustee being allowed to be subrogated to the rights

of the creditor, under the provisions of § 67, 'Liens,' cl. 3, no question in respect to which is presented here."

In re Sentenne & Green Co., 9 A. B. R. 648, 120 Fed. 436 (D. C. N. Y.).

Indirect order of preservation—order directing sheriff to proceed to sell under the levy. In re S. Ah. Mi., 18 A. B. R. 138 (D. C. Hawaii).

Davis v. Crompton, 20 A. B. R. 53, 158 Fed. 735 (C. C. A. Pa.), quoted at § 1243¾. Also, compare, Miller v. Acid & Fertilizer Co., 21 A. B. R. 416, 211 U. S. 496, quoted, on other point at § 1489.

Goodnough Stock Co. v. Galloway, 22 A. B. R. 803, 171 Fed. 940 (D. C. Ga.): "There is provided in that subdivision [Bankr. Act, § 67f] a method whereby the lien of attachment may in proper cases be preserved for the benefit of the estate. This may be done by order of the court on due notice. No attempt, however, was made in the bankruptcy proceeding to so preserve the attachment lien of the bank for the benefit of the estate, and no such order of court has been made within the purview of the Act, and hence it cannot be insisted that the attachment lien still exists for any purpose. The statute was designed to preserve some interest acquired by virtue of the attachment, which would not pass to the trustee by virtue of the bankruptcy proceeding. * * * If the property passes at any rate to the trustee, there is no necessity for invoking the order of the court. The attachment being dissolved, the trustee is not further embarrassed in his settlement of the estate."

And a reasonable time is allowed the trustee to apply for such order.³⁷

The order of preservation is to be made by the bankruptcy court, not by the State court.

Obiter, *Miller v. Acid & Fertilizer Co.*, 21 A. B. R. 416, 211 U. S. 496: "It is inferable that the parties proceeded upon the erroneous conception that the State court, where the suit was pending, was competent to authorize the trustee; but, as no question on that subject was made below or is here raised, we may not reverse the judgment in favor of the trustee because of the absence of authority from the bankrupt court, when presumably the want of authority would have been supplied had its absence been challenged. Assuming, therefore, that the trustee was properly authorized, it follows that he was entitled to preserve and enforce the privilege or lien which arose in favor of the creditors, resulting from their pending action, even although the cause of action arose from the State law, and the application of that law was essential to secure the relief sought. To the accomplishment of this end the bankrupt law was cumulative and did not abrogate the State law." [For further quotation, see ante, § 1489.]

And the referee has jurisdiction to make the order.³⁸

But if the order is not made until after the property is surrendered by the creditor, it is, perhaps, too late; since, then, there is no longer any lien in existence to which the trustee might be subrogated.³⁹

In *re Walsh Bros.*, 28 A. B. R. 243, 195 Fed. 576 (D. C. Ia.): "The adjudication at once discharged and released the lien of the attachment, unless the court should order it preserved for the benefit of the bankrupt estate as provided in the section above quoted. That section does not prescribe when such order shall be made, nor the proceedings required to preserve the lien. The trustee was elected February 13, 1908, and no request was made by him or by any creditor to have the attachment lien preserved, and no order was made by the referee authorizing him to appear in the State court until April 13,

³⁷. *Watschke v. Thompson*, 7 A. B. R. 504 (Sup. Ct. Minn.): "Of course, action which seeks to secure the benefit a reasonable time would be permitted of the attachment." ³⁸. *Conti v. Sunseri*, 18 A. B. R. 891 for a trustee in which to acquaint himself with the facts, and to apply to the court and obtain the necessary order. ³⁹. *Davis v. Crompton*, 20 A. B. R. but until such order is obtained ap-64 (C. C. A. Pa.), quoted at § 1243/4.

following. The attachment lien had then been dissolved and released by operation of law for two months, and the trustee could only be subrogated to such rights as the attaching creditor then had, which were none. In any case wherein it is desired to preserve an attachment or execution lien upon the property for the benefit of the estate under § 67f, steps must be taken to that end before the lien is discharged. *Davis v. Crompton* (C. C. A., 3d Cir.), 20 Am. B. R. 53, 158 Fed. 735-743, 85 C. C. A. 633. The subrogation of the trustee as plaintiff in the attachment suit after the lien has been discharged does not revive the lien. The trustee therefore acquired no rights under the attachment of *P. Walsh, Sr.*"

But an order of preservation has been held not to be requisite where the lien is dissolved under § 67c, or the state courts' custody superseded, under that section, rather than under § 67 "f."

First Nat. Bk. v. Title & Trust Co., 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.): "In so far as 67 (c) is in conflict with 67 (f) the former is doubtless superseded by the latter section. But, if our construction of 67 c. is correct, the lien now under consideration was not dissolved by any of its provisions, but on the contrary, it was preserved, and the trustee, by operation of law and without any intervening court order, subrogated to the rights of the former receiver. Section 67 f, does not conflict with the view of 67 c. Section 67 f, like clauses 1, 2 and 3 of the first sentence of 67 c, relates only to liens, obtained for the benefit of less than all of the bankrupt's general creditors, and not to a lien which benefits all the creditors and the dissolution of which will result in giving priority to particular creditors. A trustee in bankruptcy is not by 67 f subrogated by mere operation of law to the rights of a levying creditor. He must obtain an order of court preserving the rights of the levying creditor for the benefit of the bankrupt's estate, as was done in *First Nat'l Bk. v. Staake*, 202 U. S. 148, 15 A. B. R. 639." This case is further quoted at §§ 1446 and 1603.

§ 1491¼. Notice on Lienor Requisite.—Notice to the lienor is requisite where the preservation of the lien is sought for under § 67 (f).⁴⁰

§ 1491½. Whether Extent of Lien Measures Extent of Trustee's Rights.—It would seem to follow, logically, that the extent of the lien preserved would measure the extent of the trustee's rights acquired by virtue of the preservation. So that, as to any surplus of value of the property over the amount of the lien, the trustee would stand in the bankrupt's shoes.⁴¹

However, it may be that all that is requisite is to establish the qualifications of the creditor as a lien creditor and that when the transfer is voidable as to him it is voidable as to all others entitled to his rights to the extent not of his loss but of their losses.

40. *Reardon v. Rock Island Plow Co.*, 22 A. B. R. 26, 168 Fed. 654 (C. C. A. Ills.), quoted at § 1489.

But an order of preservation is held, not to be necessary where the superseding of the State court's custody occurs through the operation of

§ 67 (c) rather than of § 67 (f), *First Nat. Bank v. Title & Trust Co.*, 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.), quoted at §§ 1446, 1491 and 1603.

41. See §§ 1243¼, 1243½. Also, compare, § 1225½.

§ 1492. Lien Not Preserved, Is Void as to Other Lienholders on Same Property.—And if the lien is not preserved by order, it is void as to other lienholders on the same property.

Thompson v. Fairbanks, 13 A. B. R. 437, 196 U. S. 516: "The trustee moved under § 67f * * * on notice to the defendant, for an order that the right or lien under the Ryan attachment should be preserved, so that the same might pass to the trustee for the benefit of the estate, as provided for in that section. This was denied. And unless such permission had been granted, the lien of the attachment was not preserved by the Act, but, on the contrary, it was dissolved under § 67c."

And this is so notwithstanding the dissolution of the lien is, as held in *In re Merrow*, 12 A. B. R. 615, 131 Fed. 993 (D. C. Mass.) for the benefit of the estate. Although the dissolution be for the benefit of the estate, the benefit, by the neglect of the trustee, has been relinquished to the lienholders. It is, indeed, precisely because the other liens are valid and that the lienholders and not the trustee would get the benefit of the dissolution that the lien is to be preserved. The dissolution of liens by legal proceedings under § 67 (f) was intended for the benefit of the estate, not for that of other lienholders, no matter how valid might be their own liens.

SUBDIVISION "C."

FRAUDULENT TRANSFERS WITHOUT PROOF OF TRANSFeree'S PARTICIPATION
IN FRAUD UNDER § 67 (e).

§ 1493. Third Branch of Trustee's Peculiar Title and Rights Conferred by Bankruptcy Act—Fraudulent Transfers within Four Months.—Under the last class of titles obtained by the trustee in bankruptcy, the third subject added is not comprehended within the ordinary common-law rights of creditors.⁴²

For the bankruptcy act by its peculiar provisions makes void all transfers made by a bankrupt within four months of his bankruptcy, where such transfers were made with the intent on his part to hinder, delay or defraud creditors, although the transferee in no way participated in such intent; unless such transferee shall prove, by way of defense, his own bona fides and his giving of a present, fair consideration therefor.⁴³

42. *In re Gray*, 3 A. B. R. 647, 47 App. Div. N. Y. 554 (N. Y. Sup. Ct. App. Div.).

43. Bankr. Act, § 67 (e): "All conveyances, transfers, assignments, or incumbrances of his property, or any part thereof, made or given by a person adjudged a bankrupt under the provisions of this act subsequent to the passage of this act and within four months prior to the filing of the peti-

tion, with the intent and purpose on his part to hinder, delay, or defraud his creditors, or any of them, shall be null and void as against the creditors of such debtor, except as to purchasers in good faith and for a present fair consideration; and all property of the debtor conveyed, transferred, assigned, or encumbered as aforesaid shall, if he be adjudged a bankrupt, and the same is not exempt from ex-

This simply throws upon the transferee the burden of proving good faith and present consideration, instead of throwing upon creditors the burden of proving his participation in the fraudulent intent.

In view of the fact that all property fraudulently conveyed passes to the trustee by operation of § 70 of the Act, it is evident no reason for the adding of the first sentence of this § 67 (e) could have existed had it not been that by this peculiar provision conveyances, transfers and incumbrances made by the bankrupt within the four months preceding bankruptcy are void, even if made with merely his own intent to hinder, delay and defraud creditors, unless the transferee prove his own good faith and adequate consideration. At common law and under the statutes, except this bankruptcy statute in its § 67 (e), a prima facie case for setting aside a transfer as fraudulent is not complete unless proof be made by the creditor of the transferee's participation in the fraudulent intent; and a suit to set aside a fraudulent conveyance, may fail precisely because of this inability to prove affirmatively the transferee's participation in the fraudulent intent.

By this provision of the first part of § 67 (e), then, fraudulent conveyances within the four months are voidable if made with solely the debtor's intent to hinder, delay or defraud creditors, even if there be no participation of the transferee in the intent, unless the transferee himself prove his own good faith and his giving of a present, fair consideration therefor.

§ 1494. Prima Facie Case without Proof of Transferee's Participation.—It is not necessary, then, in order to make a case for setting aside a fraudulent conveyance made within four months of bankruptcy, to prove in the first instance a participation in the fraudulent intent on the part of the person receiving the conveyance, but good faith and present, fair consideration is a defense to be pleaded and proved by the transferee.⁴⁴

execution and liability for debts by the law of his domicile, be and remain a part of the assets and estate of the bankrupt and shall pass to his said trustee, whose duty it shall be to recover and reclaim the same by legal proceedings or otherwise for the benefit of the creditors."

Section 67 (e) Covers Two Classes of Fraudulent Transfers.—It must be observed that § 67 (e) covers two classes of fraudulent transfers: First, those where the transferor's fraudulent intent alone need be proved to make out a prima facie case; second, those which are fraudulent by State law. The first class only is being considered at this place since it alone is a title peculiarly conferred by the Bankruptcy Act. The second class has already been considered in con-

nection with the "Title of the Trustee as Successor to the Creditors," ante, § 1216.

Other distinctions as to § 67 (e).

(1) The distinction is also made in one case that fraudulent conveyances made within the four months period are absolutely void upon the filing of the bankruptcy petition while those made before that time are voidable merely. In re Grohs, 1 A. B. R. 465 (Ref. Ohio). - This seems to be a misconception of the object of the statute.

(2) In another case, § 67 (e) is considered to include "frauds upon the Act" as contradistinguished from other frauds upon creditors. In re Gray, 3 A. B. R. 649, 47 App. Div. N. Y. 554 (N. Y. Sup. Ct. App.).

⁴⁴ Also, see *Friedman v. Vorhofsky*, 105 Ill. App. 414; *Shelton*, trustee,

Sherman v. Luckhardt, 11 A. B. R. 26 (Sup. Ct. Kansas, overruling *Sherman v. Luckhardt*, 9 A. B. R. 312 Sup. Ct. Kas.): "The clauses quoted from § 57 and § 60 treat alone the subject of preferences. No mention is there made of fraud. The lawmaking power dealt with the subject of fraud in clause "e" of § 67 of the act, and, in language so plain, concise, exact and unequivocal as to leave no room for doubt or construction, there inhibited all transfers of

v. Price, 23 A. B. R. 431, 174 Fed. 891 (D. C. Ala.); *Unmack v. Douglass*, 55 Atl. 12; *McNulty v. Wiesen*, 12 A. B. R. 341, 130 Fed. 1012 (D. C. Pa.): The reasoning of the court in this case is not, however, to be approved in its entirety.

And also compare, to the effect that § 67 (e) does not, at any rate, refer to payments of money, *Blakey v. Booneville Bk.*, 2 A. B. R. 462 (D. C. Ind.). This case was reversed in *Booneville Nat'l Bk. v. Blakey*, 6 A. B. R. 13, 107 Fed. 241 (C. C. A. Ind.), but not on this ground.

Inferentially, *In re Knopf*, 16 A. B. R. 445, 144 Fed. 245 (D. C. S. C.); instance, *In re Head and Smith*, 7 A. B. R. 556 (D. C. Ark.), the latter being a case where one partner sold out to another partner when the partnership was insolvent; held to be a hindering, delaying and defrauding of firm creditors in an attempt to convert firm property into individual property.

Instance, *In re Steininger Mercantile Co.*, 6 A. B. R. 68, 107 Fed. 669 (C. C. A. Ga.): Executing mortgages in behalf of favored creditors who are not pressing for payment nor asking for security, the mortgages covering all the debtor's property and being concededly made with the intent that the debtors might thereby enforce indulgence from other creditors and further advances from the mortgagees.

Instance, *In re Egan State Bk. v. Rice*, 9 A. B. R. 437, 119 Fed. 107 (C. C. A. S. Dak., affirming *In re Platte*, 6 A. B. R. 568): Chattel mortgage with power of sale, where the proceeds of the sales are not applied on the debt (no participation in the fraudulent intent appearing on the mortgagees' part).

Instance held not invalid under § 67 (e). *Chattel mortgage* within the four months and duly recorded, there being an oral agreement that the goods should be filled to customers supplied by a particular commission house and in its name and net proceeds to be applied to payment of mortgage debt, justifies no inference that the mortgage was made with intent to hinder, delay or defraud creditors. *In re Durham*, 8 A. B. R. 115, 114 Fed. 750 (D. C. Md.).

Instance held not invalid under § 67 (e): Partner pledging his insurance policies to creditor of firm with stipulation not to become firm property, all under advice of counsel—not under § 67 (e) nor fraudulent: *In re Bloch*, 15 A. B. R. 748 (C. C. A. N. Y.).

Instance, held not invalid under § 67 (e). *Coder v. Arts*, 18 A. B. R. 513, 153 Fed. 943 (C. C. A. Iowa.).

Instance, held invalid under § 67 (e) but transferee's intent not adverted to. *Henkel v. Seider*, 20 A. B. R. 773, 163 Fed. 553 (D. C. N. Y.): Voluntary transfers to wives to avoid creditors.

Instances, *In re Pease*, 12 A. B. R. 66, 129 Fed. 446 (D. C. Mich.): Chattel mortgage executed within four months period, for presently passing consideration, namely, a loan to be used in making preferential payments, known by mortgagee or of which he had reasonable grounds for inference, is void under § 67 (e).

Instance, *Clingman v. Miller*, 20 A. B. R. 360, 160 Fed. 326 (C. C. A. Kans.), although this was also under the last clause of § 67 (e) as well as under the first clause, and therefore properly appearing also at § 1269, where it can be found; the court in this case holding that where an insolvent debtor, in a jurisdiction where the statute provides that every general assignment shall be for the benefit of all the creditors of the assignor, on the same day that he made a general assignment for creditors, transferred certain property to a particular creditor by a separate instrument, the trustee in bankruptcy, in a suit to recover the value of property transferred to the particular creditor, is entitled to go to the jury on the question whether the transfer was a part of the transaction which resulted in the making of the general assignment, so as to make the transfer void both under the State law and also under § 67 (e) of the Bankruptcy Act, 1898, and the direction of a verdict against the plaintiff constitutes reversible error.

Contra, obiter, in *Jacobs v. Van Sicke*, 11 A. B. R. 470 (C. C. A. N. J.). And see contra, to main proposition, note to *In re McLam*, 3 A. B. R. 245, 97 Fed. 925. Also, contra, compare, under law of 1867, *Tiffany v. Lucas*, 15 Wall. 410.

the property of an insolvent debtor made within four months prior to the institution of bankruptcy proceedings under the act wherein the debtor, with the intent on his part of hindering, delaying or defrauding his creditors, parted with his property regardless of the knowledge of or participation in such fraud by the creditor. This is a case of first instance in this State in construing the above provisions of the act. In other jurisdictions a like view of the act has been reached. *Friedman v. Verchofsky*, 105 Ill. App. 414; *Unmack v. Douglass* (Conn.), 55 Atl. 12. There are cases holding a contrary view. *Congleton v. Schreihofer* (N. J. Ch.), 54 Atl. 144; *Gamble v. Elkin* (Pa.), 54 Atl. 782. However, the reasoning employed in these cases, contrary to the view expressed in this opinion, does not commend itself to our judgment or meet our approval. Such a construction of the act would nullify one of its most important and beneficial provisions."

In *re McLam*, 3 A. B. R. 245, 97 Fed. 922 (D. C. Vt.): "The provision of the latter act is more prohibitive than that of the former, for no reasonable cause of belief of insolvency and fraud on the act, by the person receiving the preference, is necessary to avoid it. The purpose and intent of the bankrupt only is looked at, and if contrary to the act, is sufficient."

In *re Moody*, 14 A. B. R. 276, 131 Fed. 525 (D. C. Iowa): "By the plain language of this section, if Moody intended by the sale to hinder, delay or defraud his creditors, the conveyance is null and void as to such creditors, except as against good faith purchasers for a present, fair consideration. It is not necessary that the purchaser should participate in the fraudulent purpose of Moody to render the transaction void as against the trustee. Such purpose being shown it must then be made to appear that the purchase was in good faith, and for a present fair consideration, paid at the time of such purchase."

In *re Hill*, 15 A. B. R. 499, 140 Fed. 984 (D. C. Calif.): "The evidence is, in my opinion, sufficient to justify the finding of the referee that the intention of the bankrupt in executing the mortgage was to hinder, delay, and defraud his other creditor. It is clear from the evidence that it was the bankrupt's intention in executing this mortgage to give a preference to the petitioner. Such an intent upon his part is one 'to hinder, delay, or defraud his creditor,' within the meaning of subdivision 'e' of § 67 of the Bankruptcy Act; and, in determining whether a conveyance or transfer of property made by a bankrupt was in violation of that section, 'the purpose and intent of the bankrupt only is looked at, and, if contrary to the Act, is sufficient' to render such conveyance or transfer void."

The commonly recurring instance of an insolvent merchant selling out his entire stock in trade for less than fair value and to close out;⁴⁵ and the selling out of the entire stock of a retail merchant without inventory,⁴⁶ have been held in several cases to come under this section, throwing the burden of proof of bona fides upon the purchaser.

§ 1495. But Transferee's Good Faith and Valuable Consideration, Defense.—But that the transferee was acting bona fide and gave a present, fair consideration is a defense.⁴⁷

⁴⁵. In *re Moody*, 14 A. B. R. 272, 134 Fed. 631 (D. C. Iowa). To same effect, compare, *Allen v. McMannes*, 19 A. B. R. 276, 156 Fed. 615 (D. C. Wis.), quoted at § 1216; In *re Rosenberg*, 22 A. B. R. 900 (Ref. N. Y.). See ante, § 1270½.

⁴⁶. In *re Knopf*, 16 A. B. R. 432 (D. C. S. C.); In *re Rosenberg*, 22 A. B. R. 900 (Ref. N. Y.). See ante, § 1270½.

⁴⁷. *Dokken v. Page*, 17 A. B. R. 228, 147 Fed. 439 (C. C. A. N. Dak.); *Shelton, trustee, v. Price*, 23 A. B. R. 431, 174 Fed. 891 (D. C. Ala.); *Meservey v.*

McNulty v. Wiesen, 12 A. B. R. 341, 130 Fed. 1012 (D. C. Pa.): "Nor is the averment in the answer that the assignment was made to the respondents without any intent on their part to hinder, delay or defraud the creditors of the bankrupt impertinent, for the reason that under § 67e * * * they are required to show that they are purchasers of these accounts in good faith, and for a present, fair consideration."

In *re Moody*, 14 A. B. R. 276, 134 Fed. 631 (D. C. Iowa): "Such purpose (transferor's fraudulent purpose) * * * being shown, it must then be made to appear that the purchase was in good faith, and for a present, fair consideration, paid at the time of such purchase."

And the burden of proof of such good faith is on the transferee.⁴⁸ And a presently passing consideration must have been given.⁴⁹

Where the consideration moving from the transferee is purely executory, his innocence will not suffice.⁵⁰

§ 1496. What Constitutes "Good Faith."—The standard of good faith as a defense for the transferee under § 67 (e) is the same as that of a creditor in accepting payments or transfers of property as payment or as security from an insolvent debtor.⁵¹

In *re Moody*, 14 A. B. R. 276, 134 Fed. 631 (D. C. Iowa): "And it is uniformly held that each (a creditor or purchaser), when dealing with one who is in fact insolvent and may be adjudged a bankrupt within four months, to exercise ordinary prudence and diligence to ascertain whether or not such insolvent can make a transfer of his property to him that will not be in violation of the Bankruptcy Law."

Thus, transactions known by the purchaser to be out of the usual and ordinary course of business tend to negative good faith; such as the sale of an entire stock of goods at less than cost.⁵²

Walburn v. Babbit, 16 Wall. 577: "But it is wholly a different thing when he sells his entire stock to one or more persons. This is an unusual occurrence, out of the ordinary mode of transacting such business, is prima facie evidence of fraud, and throws the burden of proof on the purchaser to sustain the validity of his purchase. * * *

"But the law will not let him escape in this way. The question raised by the statute is not his actual belief, but what he had reasonable cause to believe. In purchasing in the way and under the circumstances he did, the law told him that a fraud of some kind was intended on the part of the seller, and he was put on inquiry to ascertain the true condition of Mendelson's [the bankrupt vendor] business. This he did not do, nor did he make any attempt in that

Roby, 28 A. B. R. 529, 198 Fed. 844 (C. A. Colo.); *Ogden v. Reddish*, 29 A. B. R. 531, 200 Fed. 977 (D. C. Ky.); In *re Mahland*, 26 A. B. R. 81, 184 Fed. 743 (D. C. N. Y.).

48. *Horner-Gaylord Co. v. Miller & Bennett*, 17 A. B. R. 257, 147 Fed. 295 (D. C. W. Va.); In *re Rosenberg*, 22 A. B. R. 900 (Ref. N. Y.). See ante, § 1270½.

49. Impliedly, *Henkel v. Seider*, 20 A. B. R. 773, 163 Fed. 553 (D. C. N. Y.).

50. See ante, § 1219½.

51. See ante, § 1216; compare, *Wright v. Sampter*, 18 A. B. R. 355, 152 Fed. 196 (D. C. N. Y.). Compare rules post, § 1504.

52. In *re Moody*, 14 A. B. R. 272, 134 Fed. 631. (D. C. Iowa). Compare, § 1504; In *re Rosenberg*, 22 A. B. R. 900 (Ref. N. Y.). See ante, § 1270½.

direction. Indeed, he contented himself with limiting his inquiries to the object Mendelson had in selling out, and to his future purposes. Something more was required than this information to repel the presumption of fraud which the law raised in the mere fact of a retail merchant selling out his entire stock of goods. If this sort of information could sustain the sale, the provision of the bankrupt law we are considering would be no protection to creditors, for any one in Mendelson's situation, and with the purpose he had in view, would be likely to give the party with whom he was dealing a plausible reason for his conduct. The presumption of fraud arising from the unusual nature of the sale in this case can only be overcome by proof on the part of the buyer that he took the proper steps to find out the pecuniary condition of the seller. All reasonable means, pursued in good faith, must be used for this purpose. If Summerfield [the vendee] had employed any means at all directed to this end, he would have discovered the actual insolvency of Mendelson. In choosing to remain ignorant of what the necessities of his case required him to know, he took the risk of the impeachment of the transaction by the assignee in bankruptcy, in case Mendelson should, within the time limited in the statute, be declared a bankrupt."

Dokken v. Page, 17 A. B. R. 228, 147 Fed. 438 (C. C. A. N. Dak.): "The claim of the intervener is a palpable fraud on the Bankrupt Act. It is full time that speculating purchasers from insolvent debtors should know that under the bankrupt act they cannot stop their ears and shut their eyes lest they may hear or see that such a merchant as Tveten was selling out his entire stock of goods in order to defeat his creditors in the collection of their just claims. Such speculators on chance seem to think that they can escape the statute by studiously and cunningly placing themselves in a position to half satisfy conscience by saying:

"I did not know the vendor was bankrupt. He did not so inform me; and I did not ask him. I did not know about his creditors, as I did not examine his books. I did not take an inventory of the goods or carefully examine them, as I had a general knowledge of their character, and did not look further"—and the like.

"Under the Bankrupt Act such a purchaser, within the four months' limitation, is presumptively a purchaser with knowledge. To protect his purchase the burden rests upon him to show satisfactorily that he was a purchaser in good faith; that he paid a present, fair consideration for the property; and that he did not know or have reason to believe that the vendor was insolvent."

Although the mere fact that the sale was one out of the usual course of business is not of itself *prima facie* proof of fraudulent intent, but merely a badge to be taken into consideration along with other facts.

Houck v. Christy, 18 A. B. R. 330, 152 Fed. 612 (C. C. A. Kans.): "It may be that, in the recent case of *Dokken v. Page* (C. C. A.), 17 Am. B. R. 228, 147 Fed. 438, involving a sale by a retail merchant of his entire stock of goods, we gave undue prominence to the language of the court in *Walbrun v. Babbitt*; but it was not our intention to say that the fact that the sale was out of the usual and ordinary course of business was, when taken alone, *prima facie* evidence of fraud under the present Bankruptcy Act, but only that it was a circumstance which, in connection with the surrounding facts disclosed in the opinion, vitiated the sale there under consideration."

Thus, a purchaser is not in good faith where he willfully closes his eyes to information with his reach.⁵³

Thus, likewise, purchasers from one known to be insolvent, or purchasing an entire stock at less than cost, are put upon inquiry, and are bound to investigate, and are not exercising good faith if they do not investigate.⁵⁴

Houck v. Christy, 18 A. B. R. 330, 152 Fed. 612 (C. C. A. Kans.): "One is not a purchaser in good faith, if he purchases with knowledge of the fraudulent intent of the vendor, or under such circumstances as should put him upon inquiry as to the object for which the vendor sells. *Jones v. Simpson*, 116 U. S. 609, 614, * * *. Apart from what Christy had learned through his connection with the bank, he and Cover knew that Stephenson was engaged in a business in which men usually have creditors, that he had been recently incumbering his property for small amounts, that he was hastily disposing of all of it for much less than its fair value, that he was insisting that he be paid in cash, which it is easy to conceal from creditors, and that the transaction was altogether unusual. Plainly, therefore, they had knowledge of what reasonably should have put them, as prudent men, upon inquiry as to his solvency and purpose, and were chargeable with all the knowledge which would have been acquired by prosecuting the inquiry with reasonable diligence; which they did not do."

In re Levine, 28 A. B. R. 481, 196 Fed. 589 (D. C. N. Y.): "To allow a creditor to invest the amount of his debt in a partnership business, and to receive in exchange stock of a corporation organized to take over that business, and then to allow the corporation to buy back that stock by the giving of a chattel mortgage upon the assets and by the payment of cash, when all of the parties had knowledge of the entire transaction, and when the business was at all times insolvent, is a plain fraud upon all of the creditors."

And it has apparently been held that a mortgagee who gives present and adequate consideration but who knows the proceeds are to be used to defeat the purpose of the Bankrupt Act, as, for instance, to create, indirectly, a preference, is not acting in "good faith" in the transaction, and that his mortgage is voidable.⁵⁵

But where adequate consideration was given, and the sale was talked of for a long time beforehand and everything appeared fair and above board, the transferee's good faith has been held established.⁵⁶

It has been held in Maine that a purchaser in good faith of an entire stock of merchandise in bulk is protected even where there has been failure to comply with the Anti Bulk-Sales-Act, such act not making such sale fraudulent in law.⁵⁷

More than merely the delaying of creditors is requisite; and where the transfer is based upon a presently passing consideration, it will not be void-

⁵³. *Lumpkin v. Foley*, 29 A. B. R. 685, 204 Fed. 378 (C. C. A. Ga.).

⁵⁴. *Dokken v. Page*, 17 A. B. R. 228, 147 Fed. 439 (C. C. A. N. Dak.); *In re Moody*, 14 A. B. R. 272, 134 Fed. 631 (D. C. Iowa). Also, see *Wager v. Hall*, 16 Wall. 584; *Walburn v. Bab-bitt*, 16 Wall. 577; *In re Rosenberg*, 22

A. B. R. 900 (Ref. N. Y.). See ante, §§ 1227, 1270½.

⁵⁵. *Roberts v. Johnson*, 18 A. B. R. 136, 151 Fed. 567 (C. C. A. Md.).

⁵⁶. *In re Bartlett*, 22 A. B. R. 891, 172 Fed. 679 (D. C. Pa.).

⁵⁷. *Gorham v. Buzzell*, 24 A. B. R. 440, 178 Fed. 596 (D. C. Maine.).

able for fraud unless it actually hinders or defrauds creditors and unless the transferee knew or had reasonable notice when he took it that it was intended to hinder or defraud the creditors of the transferor, or was made in contemplation of or fraud of the bankruptcy law; and in the absence of such knowledge or notice the fact that the lien or other transfer actually hinder creditors by withdrawing securities or property from application to the payment of their debt is insufficient to avoid it.⁵⁸

§ 1496 $\frac{1}{4}$. Badges of Fraud Considered All Together, Not Separately.—Badges of fraud altogether inconclusive if separately considered, may, by their number and joint operation, be sufficient to constitute conclusive proof of fraudulent intent on the part of both transferor and transferee.⁵⁹

§ 1496 $\frac{1}{2}$. Great Latitude in Admission of Evidence.—Questions of fraud can scarcely ever be proved by direct evidence, hence the necessity for admission of all circumstances fairly connected with the transaction.⁶⁰

Lumpkin v. Foley, 29 A. B. R. 673, 204 Fed. 373 (C. C. A. Ga., aff'g *In re Walden Bros. Clothing Co.*, 29 A. B. R. 80, 199 Fed. 315, D. C. Ga.): "Fraud is not to be presumed, but that does not imply that fraud may not be proved by circumstances as well as by direct evidence. Fraud may be actual arising from facts and circumstances of imposition. It may be apparent from the intrinsic nature and subject of the bargain itself. *Hume v. U. S.*, 132 U. S. 406.

"The testimony of the witnesses considered by the referee in connection with all the circumstances, taken with Lumpkin's testimony, satisfied the referee that the claimant shut his eyes to the situation, and we cannot say that the referee is wrong in his contention that Lumpkin tacitly acquiesced in a subtle scheme between the bankrupt and the favored few of its creditors.

"As was said by Mr. Justice Day in *Wecker v. National Enameling Co.*, 204 U. S. 182: 'In cases where the direct issue of fraud is involved, knowledge may be imputed where one willfully closes his eyes to information within reach.'

"There seems to be no dearth of authority that a purchaser is not in good faith who makes no effort to determine whether one may make a transfer which will not be in violation of the Act. *Houck v. Christy* (C. C. A., 8th Cir.), 18 Am. B. R. 330, 152 Fed. 615; *Dokken v. Page* (C. C. A., 8th Cir.), 17 Am. B. R. 228, 147 Fed. 439, 77 C. C. A. 674; *Shauer v. Allerton*, 155 U. S. 607; *Harrell v. Beall*, 17 Wall. 590."

§ 1497. Section 67 (e) Not Applicable to Mere Preferential Transfers.—Section 67 (e) does not apply to mere preferential transfers.⁶¹

58. *Powell v. Gate City Bank*, 24 A. B. R. 316, 178 Fed. 609 (C. C. A. Mo.).

59. *Houck v. Christy*, 18 A. B. R. 330, 152 Fed. 612 (C. C. A. Kans.), quoted at § 1496; also, see ante, §§ 109, 1216 $\frac{1}{2}$.

60. *In re Luber*, 18 A. B. R. 476, 152 Fed. 492 (D. C. Pa.), quoted at § 114 $\frac{1}{2}$.

61. *In re Varley, etc., Co.*, 26 A. B. R. 840, 188 Fed. 761 (D. C. Ala.); *Mc-*

Atee v. Shade, 26 A. B. R. 151, 185 Fed. 442 (C. C. A. Mo.); *In re Kullberg*, 23 A. B. R. 758, 176 Fed. 585 (D. C. Minn.); *In re Bloch*, 15 A. B. R. 748, 142 Fed. 674 (C. C. A. N. Y.).

Contra, *In re Jones*, 9 A. B. R. 262 (D. C. S. C.): In this case a preference was held to be voidable under 67 (e) without participation of the transferee in the intent. This decision was manifestly placed upon the wrong

Van Iderstine, trustee, *v.* Nat'l Discount Co., 23 A. B. R. 345, 174 Fed. 518 (C. C. A. N. Y.): "There is a marked distinction between a preferential payment and a fraudulent conveyance. Every preferential payment must to some extent hinder and delay creditors, but it is not necessarily a fraudulent conveyance. * * * A preferential payment may be constructively fraudulent, but it is not in and of itself a fraudulent conveyance. It can only become the latter in the unusual case where actual fraud in addition to the preferences is established. Thus a secret trust in favor of a person making such payments might turn a mere preference into a fraudulent conveyance. But there is no proof in this case of any intent to hinder or defraud creditors more than the preferential payments in themselves would have hindered them."

Coder *v.* Arts, 213 U. S. 223, 22 A. B. R. 1: "A consideration of the provisions of the bankruptcy law as to preferences and [fraudulent] conveyances shows that there is a wide difference between the two, notwithstanding they are sometimes spoken of in such a way as to confuse the one with the other. A preference, if it have the effect prescribed in § 60, of enabling one creditor to obtain a greater portion of the estate than others of the same class, is not necessarily fraudulent. Preferences are set aside when made within four months, with a view to obtaining an equal distribution of the estate, and in such cases it is only essential to show a transfer by an insolvent debtor to one who himself or by his agent knew of the intention to create a preference. In construing the Bankruptcy Act this distinction must be kept constantly in mind. As was said in *Githens v. Shiffler* (D. C.), 7 Am. B. R. 453, 112 Fed. 505: 'An attempt to prefer is not to be confounded with an attempt to defraud, nor a preferential transfer with a fraudulent one.' In *re Maher*, 16 A. B. R. 343, 144 Fed. 503-509, it was well said by the district court of Massachusetts: 'In a preferential transfer the fraud is constructive or technical, consisting in the infraction of that rule of equal distribution among all creditors which it is the policy of the law to enforce when all cannot be fully paid. In a fraudulent transfer the fraud is actual—the bankrupt has secured an advantage for himself out of what in law should belong to his creditors, and not to him.'"

Sargent *v.* Blake, 20 A. B. R. 115, 160 Fed. 57 (C. C. A. Me.): "Intentional transfers by insolvents to secure or pay pre-existing debts within four months prior to the filing of a petition in bankruptcy which are not voidable as preferences under § 67e, or violative of other provisions of law, and which are made without intent to hinder, delay, or defraud creditors more than such securities or payments necessarily have that effect, do not evidence an intent to hinder, delay, or defraud creditors within the meaning of § 67e of the Bankruptcy Act of 1898. It is not every intent to hinder or delay creditors in collecting, or to prevent them from collecting, but, an intent to do so unlawfully only that is denounced by that section."

Coder *v.* Arts, 18 A. B. R. 513, 152 Fed. 943 (C. C. A. Iowa, affirmed in Coder *v.* Arts, 22 A. B. R. 1, 213 U. S. 223: "A transfer by an insolvent, within four months prior to the filing of a petition, for the purpose of securing or paying a pre-existing debt, without any intent or purpose to affect other creditors injuriously beyond the necessary effect of the security, is lawful, if

ground. It was not voidable under 67 (e) for the reason that it was a conveyance made to hinder, delay or defraud creditors, but was simply a preference voidable under 60 (b). The court evidently labored under a confusion between the intent to prefer and the intent to defraud, as to

which see *In re Duffy*, 9 A. B. R. 358; *Githens v. Shiffler*, 7 A. B. R. 453, 112 Fed. 505, and ante, §§ 1397, 1221, 113.

But also compare, *Spencer v. Nekemoto*, 24 A. B. R. 517 (D. A. Hawaii), which also seems rather to have been merely a case of preference, though held voidable on both grounds.

not violative of other provisions of law, and it does not evidence any intent to hinder, delay, or defraud creditors within the meaning of Bankruptcy Act, 1898, § 67e."

§ 1498. And Trustee Must Show Bankrupt's Actual Fraud.—

And the trustee must, of course, as part of his case in chief show the bankrupt's fraud in making the transfer.⁶²

Coder v. Arts, 213 U. S. 223, 22 A. B. R. 1: "But the act does not dispense with the necessity of showing, to avoid a conveyance or transfer under § 67e, that the bankrupt had the actual intent to hinder, delay, or defraud creditors. What is meant when it is required that such conveyances, in order to be set aside, shall be made with the intent on the bankrupt's part to hinder, delay, or defraud creditors? This form of expression is familiar to the law of fraudulent conveyances, and was used at the common law, and in the statute of Elizabeth, and has always been held to require, in order to invalidate a conveyance, that there shall be actual fraud; and it makes no difference that the conveyance was made upon a valuable consideration, if made for the purpose of hindering, delaying, or defrauding creditors. The question of fraud depends upon the motive. *Kerr, Fraud & Mistake*, 196, 201. The mere fact that one creditor was preferred over another, or that the conveyance might have the effect to secure one creditor and deprive others of the means of obtaining payment, was not sufficient to avoid a conveyance; but it was uniformly recognized that, acting in good faith, a debtor might thus prefer one or more creditors. *Stewart v. Dunham*, 115 U. S. 61, * * * *Huntley v. Kingman & Co.*, 152 U. S. 527, * * * We are of opinion that Congress, in enacting 67e, and using the terms 'to hinder, delay, or defraud creditors,' intended to adopt them in their well-known meaning as being aimed at conveyances intended to defraud. In § 60 merely preferential transfers are defined, and the terms on which they may be set aside are provided; in 67e, transfers fraudulent under the well recognized principles of the common law and the statute of Elizabeth are invalidated. The same terms are used in § 3, subdivision 1, in which it is made an act of bankruptcy to transfer property with intent to hinder, delay, or defraud creditors. Such transfers have been held to be only those which are actually fraudulent."

Thompson v. Fairbanks, 196 U. S. 516, 13 A. B. R. 443: "There is no finding that in parting with the possession of the property, the mortgagor had any purpose of hindering, delaying or defrauding his creditors or any of them. Without a finding to the effect that there was an intent to defraud, there was no invalid transfer of the property under the provisions of § 67 (e) of the Bankruptcy Law."

The rule of 67 (e) simply relieves the trustee from the necessity, otherwise existing, of showing the transferee's participation therein.

§ 1499. Transfer Must Have Been within Four Months.—

The transfer must have been made within the four months preceding the filing of the bankruptcy petition to be voidable, if the transferee's participation in the fraudulent intent be not shown.⁶³

⁶². *Meservey v. Roby*, 28 A. B. R. 529, 198 Fed. 844 (C. C. A. Colo.); impliedly, *In re Bloch*, 15 A. B. R. 748, 142 Fed. 676 (C. C. A. N. Y.).

⁶³. Impliedly, *In re Hill*, 15 A. B.

R. 499, 140 Fed. 981 (D. C. Calif.); impliedly, *Henkel v. Seider*, 20 A. B. R. 773, 163 Fed. 553 (D. C. N. Y.); *Underleak v. Scott*, 28 A. B. R. 926 (Sup. Ct. Minn.).

But if made on the same day of the month of the fourth month preceding, it is "within four months."⁶⁴

Voluntary conveyances by way of gift, to avoid creditors, are not limited to four months and do not have to come under § 67 (e).⁶⁵ They are void under Bankruptcy Act, § 70 (a) (4), being "property transferred by him in fraud of his creditors," title to which passes to the trustee by operation of law.

§ 1499½. Insolvency, Whether Requisite.—Insolvency is not a requisite element, under the first clause of § 67 (e), though generally necessary as evidence towards establishing fraudulent intent.⁶⁶

Obiter, *Spencer v. Nekemoto*, 24 A. B. R. 517 (D. C. Hawaii): "Under the allegation that the payment to Nekemoto was made with the intent to hinder, delay and defraud his creditors, proof of insolvency is not essential, under § 67 (e), covering this point, although insolvency would appear to be generally an existing condition where there is an attempt to defraud creditors."

DIVISION 4.

PROTECTION OF LIENS WHICH ARE NOT CONTRARY TO THE BANKRUPT ACT.

§ 1500. Protection of Liens Which Are Not in Contravention of Act.—"Liens given or accepted in good faith and not in contemplation of or in fraud upon the act and for a present consideration, which have been recorded according to law, if record be necessary to impart notice, are, but to the extent of such present consideration only, not affected."⁶⁷

Liens given at any time before the filing of the petition upon a presently passing consideration, that is to say, not in payment of a pre-existing debt—not in consideration, in other words, of a reduction of liabilities, but in consideration of the contemporaneous increase or at least replacing of assets—are valid, if they are given or accepted in good faith and not in contemplation of or fraud upon the Bankruptcy Law, and if, also, they have been duly recorded where the State laws require recording in order to impart notice.⁶⁸

^{64.} *In re Hill*, 15 A. B. R. 499, 140 Fed. 981 (D. C. Calif.).

^{65.} *In re Scheuch*, 8 A. B. R. 727, 116 Fed. 535 (D. C. Wash.); *In re Toothacker Bros.*, 12 A. B. R. 99, 128 Fed. 187 (D. C. Conn.).

^{66.} Compare ante, §§ 116, 1218¼.

^{67.} Bankr. Act, § 67 (d), as amended in 1910: "Liens given or accepted in good faith and not in contemplation of or in fraud upon this act, and for a present consideration, which have been recorded according to law, if record thereof was necessary in order to impart notice, shall, to the extent of such present consideration only, not be ef-

fectured by this act." See cases involving liens under various subjects ante and post, "Title of Trustee as Successor to Bankrupt," "Fraudulently Conveyed Property," "Preferences," etc. Necessarily the subject of valid liens would be involved in many such cases and other cases.

McDonald v. Taylor & Co., 26 A. B. R. 635 (App. Div. N. Y.); *In re Stroum*, 27 A. B. R. 721, 192 Fed. 762 (C. C. A. Mass.).

^{68.} *In re Wolf*, 3 A. B. R. 555, 98 Fed. 84 (D. C. Iowa); *Tiffany v. Boatman's Inst.*, 18 Wall. 375; *Crim v. Woodford*, 14 A. B. R. 302, 136 Fed. 34 (C. C. A.

Hiscock v. Varick Bk., 18 A. B. R. 9, 206 U. S. 28: "The contracts under which they were pledged were valid and enforceable under the laws of New York where the debt was incurred and the lien created. The Bankruptcy Act did not attempt by any of its provisions to deprive a lienor of any remedy which the law of the State vested with him; on the other hand, it provided, § 67 (d) etc."

Ridgeway v. Kendrick, 31 A. B. R. 497, 208 Fed. 849 (C. C. A. N. J.): "And it cannot be avoided as a fraudulent lien because the evidence shows that it was recorded according to law, and was both given and accepted 'in good faith and not in contemplation of, or in fraud upon this act, and for a present consideration.' It is, therefore, protected by Bankruptcy Act § 67d as amended 1910."

In *re Soudan's Mfg. Co.*, 8 A. B. R. 45 (C. C. A. Ind.): "It is equally clear that § 67 (d) saves from invalidity the security thus founded upon a present consideration if accepted in good faith and not in contemplation of or in fraud upon the Act, and in the absence of notice which impeaches the good faith of the transaction as so defined the mortgagee is entitled to the benefits of his lien notwithstanding the fraud, if any there was, on the part of the mortgagor."

Darby v. Inst., 1 Dill. 144, Fed. Cas. 3571: "An insolvent person may properly make efforts to extricate himself from his embarrassment, and therefore he may borrow money, and give at the time security therefor, provided, always, the transaction be free from fraud in fact, and upon the Bankrupt Act. And hence it is a settled principle of bankrupt law, both in England and in this country, that advances made in good faith to a debtor to carry on business, upon security taken at the time, do not violate either the terms or policy of the Bankrupt Act."

In *re Porterfield*, 15 A. B. R. 11, 138 Fed. 192 (D. C. W. Va., reversed, on other grounds, sub nom. *Moore v. Green*, 16 A. B. R. 651, 145 Fed. 480): "Both the State and Bankrupt Act recognize the right to make a transfer giving preference for a new, and not an existing consideration or debt, if made in good faith."

Stedman v. Bk. of Monroe, 9 A. B. R. 4, 117 Fed. 237 (C. C. A. Iowa): "But no such result followed in respect to the \$3000 actually loaned when the mortgage was given. As to that sum the security of the mortgage was valid under the terms of § 67d unless it was given in contemplation of bankruptcy or in fraud-upon the act."

In *re Brown*, 5 A. B. R. 221 (D. C. Pa.): "* * * and such liens are declared by clause 'd' of § 67 to be unaffected by the Act. The term 'unaffected' may perhaps be too broad, other sections do affect such liens in some respects not material, but the general meaning of the phrase is clear. Such liens are left as the act finds them and (passing the question whether the Court may in-

W. Va.); *Bank v. Bruce*, 6 A. B. R. 312, 109 Fed. 69 (C. C. A. S. C.); In *re Clifford*, 14 A. B. R. 283, 136 Fed. 475 (D. C. Iowa); *Davis v. Turner*, 9 A. B. R. 705, 716, 120 Fed. 605 (C. C. A. N. Car.); *obiter*, *Farmers' Bk. of Edgefield v. Carr*, 11 A. B. R. 733, 127 Fed. 690 (C. C. A. S. Car.); *instance*, In *re Cobb*, 3 A. B. R. 129, 96 Fed. 821 (D. C. N. Car.); *impliedly*, In *re U. S. Food Co.*, 15 A. B. R. 329 (Ref. Mich.); *obiter*, *Roberts v. Johnson*, 18 A. B. R. 135, 151 Fed. 567 (C. C. A. Md.); *obiter*, In *re Wright*, 2 A. B. R. 366, 96 Fed. 187 (D. C. Ga.); *Ohio Val-*

ley Bank Co. v. Mack, 20 A. B. R. 40, 163 Fed. 155 (C. C. A. Ohio); In *re Hersey*, 22 A. B. R. 863, 171 Fed. 1001 (D. C. Iowa); *Martin v. Orgain*, 23 A. B. R. 454, 174 Fed. 772 (C. C. A. Tex.); *impliedly*, *Simmons v. Greer*, 23 A. B. R. 443, 174 Fed. 654 (C. C. A. S. Car.); In *re Kulberg*, 23 A. B. R. 758, 176 Fed. 585 (D. C. Minn.); *Vollmer v. Plage*, 26 A. B. R. 590, 186 Fed. 598 (D. C. N. Y.); *McAtee v. Shade*, 26 A. B. R. 151, 185 Fed. 442 (C. C. A. Mo.); *Powell v. Gate City Bank*, 24 A. B. R. 317, 178 Fed. 609 (C. C. A. Mo.).

terfere in the case of a fraudulent or oppressive enforcement) they may be proceeded upon according to their terms." But the court in *In re Brown* implies that the burden of showing bad faith is upon the trustee. The facts do not disclose whether the transfer was within the four months period or not.

Am. Mach. Co. v. Norment, 19 A. B. R. 679, 157 Fed. 801 (C. C. A. N. C.): "This deed of trust having been executed within four months of the bankruptcy adjudication can only be maintained on the ground that the debt secured thereby was made in good faith and without fraud to secure a present advancement or loan of money to the bankrupt company, and therefore saved by subdivision 'd' of § 67 of the Bankrupt Act."

Thus, an embarrassed debtor may borrow money and give a mortgage to carry on his business, and if the lender lend in good faith, his mortgage is valid.⁶⁹

Obiter, *In re Pease*, 12 A. B. R. 68, 129 Fed. 446 (D. C. Mich.): "The propositions that advances may be lawfully made in good faith to a debtor to carry on his business, and that the lender may lawfully take security at the time for such advances without violating the Bankrupt Act, are beyond denial."

But if the loan be in bad faith, it is void even though on a present consideration.⁷⁰

Likewise, mortgages to secure future advances are valid if made in good faith, at any rate to the amount of the advances at the time of the bankruptcy.⁷¹ It will be useful to explicate this clause in some detail.

§ 1501. Is Converse of Avoidance of Liens Opposed to Bankruptcy Act.—This provision of the law protecting certain liens is, substantially, simply the converse of other provisions of the statute invalidating certain transfers. Thus, transfers that are fraudulent as to creditors certainly are not "bona fide," so we find that the right to avoid fraudulent transfers of property, which we have heretofore discussed as one of the trustee's rights, has its converse in the protection given by § 67 (d) to "bona fide" liens. Again, the avoidance of preferences and fraudulent transfers is one of the chief objects and purposes of the Bankruptcy Act, and therefore we find, in § 67 (d) the converse of the trustee's peculiar rights conferred by the Bankruptcy Act to avoid preferences and fraudulent transfers in the provision protecting liens "not in contemplation of nor in fraud upon the Act and upon present consideration."⁷²

Compare, *Young v. Upson*, 8 A. B. R. 377, 115 Fed. 192 (D. C. N. Y.): "The security was given for a present consideration and therefore no fraud on creditors, under the Bankruptcy Act."

69. *In re Wolf*, 3 A. B. R. 555, 98 Fed. 974 (D. C. Iowa); *Davis v. Turner*, 9 A. B. R. 704, 120 Fed. 605 (C. C. A. N. C.); *In re Soudans Mfg. Co.*, 8 A. B. R. 45, 113 Fed. 804 (C. C. A. Ind.).

70. *In re Pease*, 12 A. B. R. 66, 129 Fed. 446 (D. C. Mich.); impliedly,

Roberts v. Johnson, 18 A. B. R. 135, 151 Fed. 567 (C. C. A. Md.).

71. *In re U. S. Food Co.*, 15 A. B. R. 329 (Ref. Mich.). See also, ante, "Third Element of a Preference," § 1319.

72. Compare, *In re Brown*, 5 A. B. R. 221 (D. C. Penn.).

Again, we find the converse of the right of the trustee to recover property in cases of unrecorded liens, in the exception of § 67 (d) that the liens, to be protected, must be recorded, if recording is necessary in order to impart notice. Thus, this § 67 (d), protecting certain liens, is simply the converse of other provisions of the Act prohibiting certain other transfers.⁷³

Likewise, we find the converse of the nullification of liens acquired by legal proceedings while the debtor is insolvent within four months of the bankruptcy, under § 67 (f), in the protection of liens not acquired by legal proceedings, or where the legal proceedings simply enforce a lien already existing and not acquired by legal process.⁷⁴

This provision protects assignments, given for presently passing consideration, of wages to be earned in the future under existing contracts of employment.⁷⁵

It is probable that, even had there been no specific enactment protecting such liens, yet, under the doctrine of "expressio unius exclusio alterius" bona fide, duly recorded liens, based on present consideration and not in contravention of the Bankruptcy Act, would have been protected.⁷⁶

In *re Soudans Mfg. Co.*, 8 A. B. R. 51, 113 Fed. 804 (C. C. A. Ind.): "In the Bankruptcy Act of 1867 no express provision appeared for this class of security, but in *Tiffany v. Institution*, 18 Wall. 375, 388, 21 L. Ed. 868, the Doctrine applicable to security given upon a present consideration was thus stated: * * *

"There is nothing in the Bankrupt Law which interdicts the lending of money to a man in Darby's condition (an insolvent), if the purpose be honest, and the object not fraudulent. And it makes no difference that the lender had good reason to believe the borrower to be insolvent, if the loan was made in good faith, and without any intention to defeat the provisions of the Bankrupt Act. It is not difficult to see that in a season of pressure the power to raise money may be of immense value to a man in embarrassed circumstances. With it he might be saved from bankruptcy, and without it financial ruin would be inevitable. If the struggle to continue his business be an honest one, and not for the fraudulent purpose of diminishing his assets, it is not only not forbidden, but is commendable."

And it must not be considered that liens which do not come within its provisions are rendered invalid by it, unless they be otherwise invalid.

Impliedly, *Coder v. Arts*, 18 A. B. R. 513, 152 Fed. 943 (C. C. A. Iowa): "And finally, mortgages or transfers, to secure pre-existing debts made within four months of the filing of a petition in bankruptcy, are legal and valid, unless voidable by reason of some provision of the bankruptcy law, or of some State laws, notwithstanding the fact that they create preferences. They are

73. Compare *McAtee v. Shade*, 26 A. B. R. 151, 185 Fed. 442 (C. C. A. Mo.), quoted at § 1504.

74. See ante, §§ 1155, 1160, 1161, 1444. Also, see *In re Robinson & Smith*, 18 A. B. R. 563, 154 Fed. 343 (C. C. A. Ill.).

75. *Citizens Loan Ass'n v. Boston, etc.*, R. Co., 19 A. B. R. 650 (Mass.), quoted at § 2678, also, see § 451.

76. *Davis v. Turner*, 9 A. B. R. 704, 120 Fed. 605 (C. C. A. N. Car.).

valid unless avoided; not void unless validated. The provision of § 67d, that liens for present considerations given and accepted in good faith shall not be affected by the bankruptcy law, does not strike down or render voidable those given and accepted for past considerations."

There is some apparent ambiguity in the use of the word "only" in the Amendment of 1910 to § 67d, whereby the possible construction might be given to this amendment that by implication all other liens except those mentioned in § 67d, as thus amended, *are* "affected" by the act. However, such is not a proper construction of the amendment. Section 67d, no more now than formerly, creates any additional right of avoiding liens; it is still merely the converse of the avoidance of liens opposed to the Bankruptcy Act. The object of the amendment is manifest. Some of the decisions had gone to the extent of holding an entire lien valid if any portion of it were given on present consideration, thus affording a ready means of defeating the Bankruptcy Law in reference to preferential liens. The true rule, even before the Amendment of 1910, was that a lien might be valid as to the part covered by presently passing consideration and yet be void as to the rest (see ante, § 1326, note), and the Amendment of 1910 simply puts the question at rest.⁷⁷

§ 1502. Lien within Four Months Valid if Other Essentials Exist.

—It will be observed that the lien may be given even during the four months period preceding bankruptcy—it may be given at any time, even up to the hour of bankruptcy, provided the other essentials, good faith, present consideration and recording, exist.⁷⁸

Obiter, In re Wright, 2 A. B. R. 366, 96 Fed. 187 (D. C. Ga.): "This shows that this paragraph refers to liens given or accepted within four months preceding the bankruptcy proceedings. Otherwise, if a lien had been given or accepted even though not for a present consideration, but for an antecedent debt, the lien would be good under all the provisions."

§ 1503. First Essential to Protection of Lien—Unless Both Parties Guilty, Lien Protected.—The lien must either be given or be accepted in good faith; that is to say, the bad faith of either party alone will be insufficient; they must both participate in the bad faith to make the lien bad on that account.⁷⁹

Thus, for instance, where the loan is made at the time and the lender has reason to suppose that the purpose of the loan is to give encouragement to the borrower, the security is upheld.⁸⁰ Thus, likewise, where a borrower is actually insolvent, but is a man of good standing, having a large number of supposedly profitable contracts and the necessity is supposed to be sim-

77. See Report No. 691 of the Senate Judiciary Committee of the 61st Congress, Second Session.

78. In re Hersey, 22 A. B. R. 863, 171 Fed. 1001 (D. C. Iowa).

79. Inferentially, Farmers' Bk. v. Carr, 11 A. B. R. 733 (C. C. A. S. C.).

80. Obiter, Sebring v. Wellington, 6 A. B. R. 673 (Sup. Ct. N. Y. App. Div., citing Tiffany v. Institution, 85 U. S. 375, and Clark v. Iselin, 88 U. S. 360).

ply to tide over temporary business embarrassment the lien will be protected.⁸¹

§ 1504. What Constitutes "Good Faith."—"Good faith" means that the creditor should not act in such a way as to intentionally defeat the Bankrupt Act, but should let the debtor have the money or property for some honest purpose.⁸²

Thus, mere knowledge of the borrower's insolvency, without more, is not enough to destroy the good faith.⁸³

Tiffany v. Boatman's Sav. Inst., 18 Wall. 376: "There is nothing in the Bankrupt Act which interdicts the lending of money to a man in Darby's condition, if the purpose be honest and the object not fraudulent. And it makes no difference that the lender had good reason to believe the borrower to be insolvent if the loan was made in good faith, without any intention to defeat the provisions of the Bankrupt Act. It is not difficult to see that in a season of pressure the power to raise ready money may be of immense value to a man in embarrassed circumstances. * * * His estate is not impaired or diminished in consequence, as he gets a present equivalent for the securities he pledges for the payment of the money borrowed. Nor in doing this does he prefer one creditor over another. * * * The preference at which the law is directed can only arise in case of an antecedent debt."

Obiter, In re Pease, 12 A. B. R. 68, 129 Fed. 446 (D. C. Mich.): "These two elements must have concurred in the transaction, to avoid the conveyance. It was not enough that the grantor was believed to be insolvent in order to defeat the title of the grantee, but it must also appear that the grantee knew that the conveyance was made with a view to effect any (some) purpose prohibited by the Act."

It has been held that the fact that neither the creditor nor debtor knew or had reason to know that the debtor was insolvent, or in failing circumstances, must be made to appear. And in some cases it has been held that such fact must be made to appear clearly and without question; ⁸⁴ although the requirement that lack of reasonable cause for believing the debtor insolvent must appear clearly and without question is probably not proper.

Impliedly, *Ohio Valley Bank Co. v. Mack*, 20 A. B. R. 40, 163 Fed. 155 (C. C. A. Ohio): "It is enough to say that the state of the evidence does not, under the principles affecting appeals upon questions of fact determined by a referee who heard the witnesses and confirmed by the district judge, warrant a refusal to accept the conclusion of the courts below that Stockhoff did not knowingly abet the bankrupt in giving a preference to Charles Mack, Sr. He stands therefore in the attitude of one who took a security for money advanced at the time in good faith. This saves his mortgage."

⁸¹ *Crim v. Woodford*, 14 A. B. R. 302, 136 Fed. 34 (C. C. A. W. Va.).

⁸² *Kaufman v. Treadway*, 12 A. B. R. 685, 195 U. S. 271. See ante, §§ 1227, 1496.

⁸³ Inferentially, In re Wolf, 3 A. B. R. 555, 96 Fed. 974 (D. C. Iowa); infer-

entially, *Crim v. Woodford*, 14 A. B. R. 310, 136 Fed. 34 (C. C. A. W. Va.). *Obiter*, *Sebring v. Wellington*, 6 A. B. R. 673 (Sup. Ct. App. Div.).

⁸⁴ *Farmers' Bk. v. Carr*, 11 A. B. R. 733 (C. C. A. S. C., citing *McNear v. McIntyre*, 7 A. B. R. 639, 113 Fed. 113).

In any event all such cases proceed on an erroneous idea of the rule. The rule is not that both parties must show good faith, but that if *either* party show bad faith, the lien will not be destroyed because of the other party's bad faith.

And, at any rate, notice of the insolvency of the borrower, to impeach the bona fides of the loan, must be based on a valuation of assets in the condition when the loan was made with the works in operation and not on the appraised value after adjudication.⁸⁵

But he is not in good faith where he willfully closes his eyes to information within reach.⁸⁶

Thus, similarly, a debtor may give a mortgage on his property or sell it to raise the money to make his statutory deposit in going into bankruptcy, and the mortgage will be good.⁸⁷ Again, a debtor may, in contemplation of voluntary bankruptcy proceedings by him or involuntary proceedings against him, prepay or secure an attorney for services to be rendered in the future in relation to the bankruptcy.⁸⁸

But where the lienholder is not acting in good faith, but is aiding a creditor to obtain a preference by a colorable transaction, the lien will not be good.⁸⁹

Thus, where the managing officers of the bankrupt corporation were also managing officers of a little bank which had so grossly overloaned to the bankrupt that the bank examiner had severely criticized them, whereupon one of the officers had endorsed the note and then afterwards had made new notes to the bank, extinguishing the original obligation, a mortgage made to him by the bankrupt at the time of the extinguishment, and withheld from record for a time though eventually filed before the bankruptcy, was held preferential and also not to have been in "good faith."

McAtee v. Shade, 26 A. B. R. 151, 185 Fed. 442 (C. C. A. Mo.): " 'Good faith,' and 'not in contemplation of or in fraud upon the Bankruptcy Act,' are of the essence of this subsection, without which the liens therein mentioned cannot be upheld even though there be a present consideration for them. We think that these essentials are lacking in the transaction of June 28th between the bank-

85. *In re Soudan Mfg. Co.*, 8 A. B. R. 51, 113 Fed. 804 (C. C. A. Ind.).

86. *Lumpkin v. Foley*, 29 A. B. R. 673, 204 Fed. 373 (C. C. A. Ga.), quoted at § 1496.

87. *In re Blanchard*, 20 A. B. R. 417, 161 Fed. 793 (D. C. N. Car.). (1867) *In re Keefer*, 4 N. B. Reg. 126.

88. Bankr. Act, § 60 (d); *Furth v. Stahl*, 10 A. B. R. 442, 205 Penn. 439; *In re Morris*, 11 A. B. R. 145, 125 Fed. 841 (D. C. N. Car.); *In re Blanchard*, 20 A. B. R. 417, 161 Fed. 793 (D. C. N. Car.).

89. *Roberts v. Johnson*, 18 A. B. R. 132, 151 Fed. 567 (C. C. A. Md.); *Hackney v. Raymond Bros. Clarke Co.*, 10 A. B. R. 213 (Neb.); compare, same case, on reconsideration and reversal,

in 13 A. B. R. 164, 68 Neb. 624. *In re Beerman*, 7 A. B. R. 431, 112 Fed. 663 (D. C. Ga.), where mortgage was given to raise money to prefer a creditor, mortgagee knowing of the proposed use and taking a bond of indemnity from the creditor. Inferentially, *In re Pease*, 12 A. B. R. 66, 129 Fed. 446 (D. C. Mich.). Compare the facts in *In re Pease*, 12 A. B. R. 148, 101 Fed. 107 (D. C. Iowa). Compare, rule protecting bona fide purchasers for value in cases of fraudulent transfers and what will not amount to bona fides in such cases, ante, § 1494; and *Houck v. Christy*, 18 A. B. R. 330, 152 Fed. 612 (C. C. A. Kans.). See ante, § 1301, et seq. *Lumpkin v. Foley*, 29 A. B. R. 685, 204 Fed. 373 (C. C. A. Ga.).

rupt and Quinn, and that the mortgage to Quinn was made by the bankrupt with intent to prefer Quinn and the Jackson Bank within the meaning of § 60b of the Bankruptcy Act, and accepted by Quinn with reasonable cause to believe that it was so intended. The property covered by the trust deeds to the bank was the same as that covered by the mortgage to Quinn. These trust deeds were made in May, 1905, but were never recorded, for the reason, as Quinn says: 'We did not want the public to know we had made so large a loan to English, therefore they were kept secret and not placed of record, and only the directors of the bank knew of them.' Quinn, English, and the other directors of the bank knew the circumstances under which these trust deeds were made; that the bankrupt was then insolvent; that they were intended by it as a preference to the bank, and were accepted by the bank with reasonable cause to believe that they were so intended. The bank, therefore, could not hold the property under the trust deeds as against the trustee in the event of bankruptcy. It was plainly the purpose, therefore, of Quinn and English by the transaction of June 28, and of July 6 following, to save to the bank the property covered by the unrecorded trust deeds (but which it had lost because of its failure to record them in due time), under the cover of a new mortgage to Quinn upon the same property for a present consideration, but which was in fact, as the trust deeds were, a preference and therefore in fraud of the bankruptcy law. The estate of the bankrupt was not enhanced in the least by this transaction, and its only purpose was to substitute Quinn as its sole creditor, instead of the bank with Quinn as guarantor of its indebtedness. It was a clever attempt to evade the provisions of the Bankruptcy Act, and if permitted to succeed would work a plain fraud upon that act. Mr. Quinn did not place his mortgage of record until August 8, 1906, at 6:10 p. m., the evening before the attachment suit of the Sturdivant Bank against the bankrupt was commenced. He says the reason that he did not record it when it was made was: 'That English requested that it be not placed of record because his interests were so interwoven with the bank that placing it on record would shatter the confidence of the community in the bank. Another reason was to give English an opportunity to consummate a deal in St. Louis.' But one conclusion can be drawn from this statement of Mr. Quinn, and that is that he knew, when he took the mortgage of June 28th, of the insolvency of the bankrupt corporation, that the mortgage was intended as a preference for his own benefit and that of the bank, and as a shield to the bankrupt while its president was negotiating a deal in St. Louis, and was to be placed of record only in case a situation should arise making it necessary to do so, and that he accepted it with that in view and with reasonable cause to believe that it was intended as a preference, and with actual knowledge that it was in contemplation of a fraud upon the Bankruptcy Act. We are, therefore, of the opinion that the mortgage to Quinn cannot be sustained under § 67d, and is void under § 60b of the Bankruptcy Act."

Lack of "good faith," it has been held, must amount to actual fraud, to effect an avoidance of a lien given on a presently passing consideration.

Powell v. Gate City Bank, 24 A. B. R. 317, 178 Fed. 609 (C. C. A. Mo.): "The loan and security were not voidable unless R. A. Clark knew or had reasonable notice that they were intended to hinder, delay, or defraud the creditors of the bank, or that they were made in contemplation of or in fraud upon the bankruptcy law. Liens accepted in good faith for a present consideration and not in contemplation of or in fraud upon that act are not affected thereby. Section 67d. The security given for a present loan is not avoided by the fact that it actually hinders or delays creditors by the withdrawal of the security from application

to the payment of their claims unless it was given with an actual intent to defraud such creditors and the recipient had actual or legal notice of that purpose. Actual fraud in which the recipient of the lien or security participates is indispensable to the avoidance of a transaction of this nature."

And, likewise, liens given for a presently passing consideration, but the proceeds of which are used in making preferences, are nevertheless good if the mortgagee is ignorant of their intended use⁹⁰ or simply knows that the proceeds are to be used to pay existing creditors, but does not know that such payment of existing creditors would work a preference.⁹¹

§ 1505. Second Essential to Protection of Lien—Not to Be Given and Accepted in Contemplation of Bankruptcy or in Fraud of Act.—The lien must not be given and accepted (for the word "or" should be construed "and" here) in contemplation of bankruptcy proceedings nor in fraud upon this Act.⁹²

The word "or" must be construed "and" here because otherwise a debtor who is about to file his petition in bankruptcy could not make an advantageous sale to any one cognizant of the fact that he is contemplating bankruptcy, although thereby a fund—already well converted into money—would be brought into the bankruptcy court much to the advantage of creditors. As long as no fraud is thus perpetrated, it is perfectly valid.⁹³

The taking of possession within the four months period of after-acquired property under a chattel mortgage covering after-acquired property, in contemplation of bankruptcy proceedings, may or may not be valid, dependent upon the state law determining whether such taking of possession reverts to the date of the original mortgage or not.⁹⁴

In States where, as in New Hampshire and Vermont, neither assignees nor administrators occupy the position of levying creditors, bankruptcy will not so operate.

Compare, *In re Peasley*, 14 A. B. R. 499, 137 Fed. 190 (D. C. N. Y.): Under New Hampshire law assignees, as for instance an administrator of an insolvent estate are neither attaching creditors nor purchasers for value.

§ 1506. Third Essential to Protection of Lien—"Present Consideration."—The lien must be given for a "present consideration."⁹⁵

⁹⁰. See ante, § 1301, et seq.; also see *In re Durham*, 8 A. B. R. 115, 114 Fed. 750 (D. C. Md.); *Davis v. Turner*, 9 A. B. R. 705, 120 Fed. 605 (C. C. A. N. Car.); *Ohio Valley Bank Co. v. Mack*, 20 A. B. R. 40, 163 Fed. 155 (C. C. A. Ohio), quoted supra.

⁹¹. Compare, *In re Kullberg*, 23 A. B. R. 758, 176 Fed. 585 (D. C. Minn.); also, compare, *Stedman v. Bank of Monroe*, 9 A. B. R. 4, 117 Fed. 237 (C. C. A.); also, compare, *In re Soudans Mfg. Co.*, 8 A. B. R. 45, 113 Fed. 804 (C. C. A.); *McAtee v. Shade*, 26 A. B. R. 151, 185 Fed. 442 (C. C. A. Mo.), quoted supra.

⁹². *In re Pease*, 12 A. B. R. 66, 129 Fed. 446 (D. C. Mich.); *McAtee v. Shade*, 26 A. B. R. 151, 185 Fed. 442 (C. C. A. Mo.), quoted at § 1504.

⁹³. Compare, *Kaufman v. Treadway*, 12 A. B. R. 685, 195 U. S. 271. *In re Blanchard*, 20 A. B. R. 417, 161 Fed. 793 (D. C. N. Car.). But compare *McAtee v. Shade*, 26 A. B. R. 151, 185 Fed. 442 (C. C. A. Mo.), quoted at § 1504.

⁹⁴. *Thompson v. Fairbanks*, 13 A. B. R. 437, 196 U. S. 516.

⁹⁵. See ante, § 1326½. *Jones v. Coates*, 28 A. B. R. 249, 196 Fed. 860 (C. C. A. Mo.); *McDonald v. Clearwater R. Co.*, 21 A. B. R. 182, 164 Fed. 1007

If it be given in part for a presently passing consideration, and in part for a pre-existing debt it is protected *pro tanto*.⁹⁶

§ 1507. Fourth Essential to Protection of Lien—"Recording" Where State Law "Requires to Impart Notice."—The lien must be recorded if the laws in force affecting the particular kind of lien involved require recording in order to impart notice. This is simply a reaffirmation of clause (a) of § 67.⁹⁷

§ 1508. Chattel Mortgages and Conditional Sales Contracts, Withheld for Time but Filed before Bankruptcy.—Chattel mortgages and conditional sales contracts, withheld from record by agreement, although recorded or filed before bankruptcy, are not void for lack of record, although they may be void as being a fraud upon creditors under the State law.⁹⁸

§ 1509. Chattel Mortgages Covering Future-Acquired Property.—The subject of the protection of a lienholder's rights as to future-acquired property is considered elsewhere.⁹⁹

(U. S. C. C. Idaho); *Simmons v. Greer*, 23 A. B. R. 443, 174 Fed. 654 (C. C. S. Car.); obiter and impliedly, *In re Bartlett*, 22 A. B. R. 891, 172 Fed. 679 (D. C. Pa.); *In re Gesas*, 16 A. B. R. 872, 146 Fed. 734 (C. C. A. Idaho).

As to the meaning of the term "present consideration" in this connection, and for cases where liens are involved, see ante, "Third Element of Preference," § 1314.

96. *In re Hersey*, 22 A. B. R. 863, 171 Fed. 1001 (D. C. Iowa). *In re Mahland*, 26 A. B. R. 81, 184 Fed. 743 (D. C. N. Y.).

As to liens given in part for presently passing consideration and in part by way of preference, being good *pro tanto* and void as to the rest, see ante, "Third Element of Preference," § 1326.

As to whether mechanics' liens, landlords' liens, etc., are given for "present consideration," see ante, §§ 1155, 1160, 1161, 1444.

As to cases where the transferee is innocent but the consideration moving from him is wholly executory, see ante, § 1219½.

97. Bankr. Act, § 67 (a): "Claims which for want of record or for other reasons would not have been valid liens as against the claims of the creditors of the bankrupt shall not be liens against his estate."

Bank v. Bruce, 6 A. B. R. 311, 109 Fed. 69 (C. C. A. S. C.); *In re An-*

drae Co., 9 A. B. R. 135, 117 Fed. 561 (D. C. Wis.).

Instance held proper place of filing, *In re Franklin*, 18 A. B. R. 218, 151 Fed. 642 (D. C. N. Car.). See ante, "Third Element of Preference," § 1379; see ante, "Liens Void for Want of Record," § 1229, et seq.

And "creditor" under Massachusetts law does not mean merely one levying process but includes a general creditor, so that the trustee may avoid such a lien though no levy has been made, as, for instance, where it is recorded in one place whilst the statute requires it to be recorded in two places. *In re McDonald*, 23 A. B. R. 51, 173 Fed. 99 (D. C. Mass.).

It has been held, although the holding is of doubtful authority that if the prior lien for which the present one was given in exchange was not recorded as required by statute the present one is avoidable as a preference, *Contra, Deland v. Miller*, 11 A. B. R. 744, 119 Iowa 368.

Rosenbluth v. DeForest, etc., Co., 27 A. B. R. 359 (Sup. Ct. Conn.); *Obiter, Dougherty v. First Nat. Bank*, 28 A. B. R. 263, 197 Fed. 241 (C. C. A. Ohio).

98. Compare *Gove v. Morton Trust Co.*, 12 A. B. R. 297, 96 App. Div. N. Y. 177 (N. Y. Sup. Ct. App. Div.). See, also, ante, this chapter, division "2," subdiv. "A," § 1222.

99. See ante, §§ 1199, 1238. Compare, *In re Medina Quarry Co.*, 24 A. B. R. 769, 179 Fed. 929 (D. C. N. Y.).

DIVISION 5.

RIGHTS OF CREDITORS AGAINST THIRD PARTIES JOINTLY OR SECONDARILY
LIABLE.

§ 1510. **Rights of Creditors against Sureties for Bankrupt, etc.**—The rights of the creditor against third parties liable jointly with the bankrupt or secondarily for him, are not impaired by the bankrupt's adjudication nor by the bankrupt's discharge.¹

§ 1511. **Applies to Secondary Liability on Obligation Itself, Not to Sureties in Court Proceedings—Attachment and Appeal Bonds Released if Liability Dependent on Judgment.**—The provision of § 16 applies only to those secondarily liable on the obligation itself and not to those who become surety for the bankrupt in court proceedings instituted against the bankrupt. Wherever the liability of the surety is dependent upon judgment being obtained against the bankrupt, as usually is the case with attachment and appeal bonds, then his discharge, preventing judgment, will prevent the surety's liability from attaching.²

Wolf v. Stix, 99 U. S. 1: "The cases are numerous in which it has been held—and, we believe, correctly—that, if one is bound as surety for another to pay any judgment that may be rendered in a specified action, if the judgment is defeated by the bankruptcy of the person for whom the obligation is assumed

1. Bankr. Act, § 16 (a): "The liability of a person who is a codebtor with, or guarantor, or in any manner a surety for a bankrupt shall not be altered by the discharge of such bankrupt." *Jacquith v. Rowley*, 9 A. B. R. 525, 188 U. S. 620.

Compare, § 33 of Act of 1867. *National Bank v. Sawyer*, 6 A. B. R. 154 177 Mass. 490; *Hoyt v. Freel*, 4 N. Bank Reg. 34, 8 Abb. Pr. (N. S.) 220.

Elsbree v. Burt, 9 A. B. R. 87 (R. I. Sup. Ct.): Stockholders' liability for corporate debts not discharged by corporation's discharge.

In re *Marshall Paper Co.*, 4 A. B. R. 469, 102 Fed. 872 (C. C. A. Mass.): This was a case of directors' and stockholders' liability.

Impliedly, *Terry v. Johnson*, 12 A. B. R. 17 (C. C. A. La.): "The court of bankruptcy, it appears, was not able to see how seizure of a stranger's property to satisfy an admitted debt of a bankrupt could harm the bankrupt or his creditors, or why, if the party whose property was seized did not complain, others should be heard to do so. It is clear to us that the demurrer to the bill is well taken. The judgment of the District Court is therefore affirmed."

Penn. Trust Co. v. McElroy, 7 A. B. R. 391 (D. C. Penn.): Guarantor of paper bound to creditor although some paper is forged or fictitious.

National Surety Co. v. Medlock, 19 A. B. R. 654 (Ga.), 58 S. E. 1131: Garnishee in libel suit bound where garnishment levied before four months period.

Bailey v. Reeves, 28 A. B. R. 850, 101 Miss. 438; *Schunack v. Art Metal Nov. Co.*, 26 A. B. R. 731, 84 Conn. 331; *Butterick Pub. Co. v. Bowen Co.*, 26 A. B. R. 718, 33 R. I. 40; *Brown Coal Co. v. Antezak*, 25 A. B. R. 898, 164 Mich. 110.

Release of Dower in Preferential Mortgage, Securing Bankrupt's Debt.—Not available to mortgagee on setting aside of mortgage. In re *Lingafelter*, 24 A. B. R. 656, 181 Fed. 24 (C. C. A. Ohio).

2. Compare, *Terry v. Johnston*, 12 A. B. R. 17 (C. C. A. La.); (1867) *Odell v. Wootten*, 4 N. B. Reg. 183, 38 Ga. 225. *Crook-Horner Co. v. Gilpin*, 23 A. B. R. 350 (Md. Ct. App.); compare, In re *Mercedes Import Co.*, 21 A. B. R. 590, 166 Fed. 427 (C. C. A. N. Y.); *Windisch-Muhlhauser Brew. Co. v. Simms*, 26 A. B. R. 714 (Sup. Ct. La.); *Wise Coal Co. v. Columbia, etc., Co.*, 27 A. B. R. 445 (Ct. App. Mo.).

the surety will be released. The obvious reason is that the event has not happened on which the liability of the surety was to depend. Of this class of obligations are the ordinary bonds in attachment suits to dissolve an attachment, appeal bonds, and the like."

Klipstein v. Allen-Miles, 14 A. B. R. 15, 136 Fed. 385 (C. C. A. Ga.): "The question is not whether the discharge of the defendant released the liability of the surety, but whether the discharge prevented the happening of the contingency upon which the liability of the surety was to arise. If no judgment can be rendered against the defendant because of the discharge in bankruptcy, then no liability exists on the part of the surety. * * * The liability of the surety on the dissolving garnishment bond is not altered by the discharge of the bankrupt defendant, but the discharge prevents the happening of the contingency on which that liability depends. * * * Moreover, we think that § 16 of the Bankrupt Act manifestly refers to co-debtors, guarantors, or sureties for the bankrupt on the same or original debt—the debt on which the release is given by the discharge."

Goyer v. Jones, 8 A. B. R. 437, 440, 79 Miss. 253: "The appellant insists that, as § 16 of the Bankrupt Law preserves the liability of any person who is in any manner a surety of a bankrupt he should have been permitted to take a judgment in the Circuit Court on the appeal bond against both M. B. and R. A. Jones, with a view of having the execution of said judgment stayed perpetually as to M. B. Jones, and for the sole purpose of enforcing the judgment as to R. A. Jones. The bond stipulates only for the payment of such judgment as may be rendered in the Circuit Court against M. B. Jones."

Likewise, where judgment against the principal is prevented through the operation of § 67 "f" annulling liens obtained by legal proceedings within four months of bankruptcy.

Klipstein v. Allen-Miles, 14 A. B. R. 15, 136 Fed. 385 (C. C. A. Ga.): "Besides this, the garnishment proceedings being had within four months prior to the bankruptcy proceedings, the surety is not relieved because of the discharge of the debtor, but because his bankruptcy avoided the lien acquired by the garnishment and destroyed the remedy by which a judgment could be recovered against the defendant, which is indispensable to make the lien of any avail to the plaintiff."

§ 1511½. **Stockholder's Liability Not Released.**—The bankruptcy of a corporation will not release a stockholder, director or officer thereof from any liability, as such, under the laws of the State or of the United States.³

§ 1512. **Creditor Entitled to All Remedies against Sureties.**—A creditor may pursue all remedies against sureties for the bankrupt.

§ 1513. **Conversely, Rights and Defenses of Sureties of Bankrupt Not Affected.**—Conversely, the rights and defenses of sureties and joint obligors of the bankrupt are not affected.⁴

3. Bankr. Act, § 4 (b) "The bankruptcy of a corporation shall not release its officers, directors or stockholders, as such, from any liability under the laws of a State or Territory or of the United States." *Firestone Co.*

v. Agnew, 21 A. B. R. 292 (N. Y.); *Elsbree v. Burt*, 9 A. B. R. 87, 24 R. I. 322; *In re Marshall Paper Co.*, 4 A. B. R. 469, 102 Fed. 872 (C. C. A. Mass.).

4. *Penn. Trust Co. v. N. Y. Elroy*, 7 A. B. R. 391 (C. C. A. Penn.), wherein

§ 1513½. Creditor's Acceptance of Composition, Whether Releases Surety.—Where the creditor is one of those whose consents in writings, etc., have enabled the bankrupt to fulfill the prerequisites of the right to make a composition, it is altogether likely that the surety is released, unless he had consented to such action. Whatever might be the case with regard to a creditor who participates in the composition for the first time after confirmation, it is manifestly an entirely different case where his own active consent has helped the bankrupt to get the majority in number and amount of claims allowed, which is the prerequisite to his right to file a petition for confirmation of composition.⁵

In *re Benedict*, 18 A. B. R. 604 (Ref. N. Y.): "While through a 'composition' the principal debtor is as completely relieved from his personal liability as he would be by a 'discharge,' yet such relief is obtained in a different manner. Relief under composition cannot be obtained without the co-operation of the creditors. The active consent of the necessary number of creditors is a condition precedent. Without this active co-operation on the part of the creditors the liability of the principal debtor would remain undischarged and the remedies of the surety unimpaired. Under the Bankruptcy Act, two methods of relief are open to the insolvent debtor. The relief to be obtained is equally effectual and complete whichever method is followed. Under the first method, the insolvent surrenders his entire property for a distribution of the entire avails among his creditors. Under the second method, he may surrender the whole, or, as in this case, only a portion of his property, and with the co-operation of the requisite number of creditors and the consent of the court, he may be equally relieved from further liability to pay his indebtedness. Such relief, while equally effectual and for many purposes of the same quality as the other, it appears to me should not be considered a 'discharge' within the meaning of § 16 and so as to destroy otherwise existing rights of other persons secondarily liable. If a surety is required to pay the debt of his principal, equity demands that he should have an opportunity to indemnify himself—at least to the full measure of the principal's ability to pay—and that if in any way the holder of the claim has co-operated to deprive him of this right, such holder should be denied recourse to the surety. This view has full sanction, it appears to me, in the *Matter of McDonald*, reported at Federal Cases, 8,753, where it was decided under the Act of 1867 that if the holder of a note assented to the 'discharge' of the maker, without the consent of the endorser, the endorser would be released. Under that act, unless an estate paid fifty per cent., the 'discharge' could only be granted upon consent of the majority in number and amount of the creditors. McDonald was unable to pay the required percentage for a discharge. He procured the written consent of the required number and value of his creditors and was discharged."

§ 1513¾. Surety's Right to Defend Attachment Suit, Where Bankrupt's Trustee Refuses.—Where the trustee of a bankrupt defendant in an attachment suit declines to defend, the surety upon the attachment bond is entitled to defend.

a guarantor was held pro tanto released by the creditor's acceptance of other security for part. In *re Benedict*, 18 A. B. R. 604 (Ref. N. Y.),

quoted at § 1513½. See cases in the following section.

5. Compare, inferentially, *Firestone Co. v. Agnew*, 21 A. B. R. 292 (N. Y.).

Bluegrass Canning Co. v. Steward, 23 A. B. R. 726, 175 Fed. 537 (C. C. A. Ky.): "Pending the suit below the canning company was adjudicated a bankrupt, and this fact was shown in the case. The creditors declined to prosecute the suit. The court below allowed the suit to go on in the name of the bankrupt upon the execution of a bond indemnifying the bankrupt against costs by J. E. Gunther, a surety upon the attachment bond, but announced that it would dismiss the case if the defendants would release the sureties upon the attachment bond. This was declined, and the motion to dismiss the suit because of the plaintiff's bankruptcy was denied. The surety upon the attachment bond had a direct interest in the successful prosecution of the suit, and, if he was willing to indemnify the bankrupt, was properly allowed to go on with the case for his own protection. The bankruptcy of the corporation did not dissolve it. 2 Clark & Marshall, Private Corporations, p. 863. While the bankrupt trustee may intervene and prosecute a pending suit if he will, yet, if he does not, we see no reason why the bankrupt may not go on with it if he wishes."

§ 1514. Right to Retain Indemnity Given at Signing Unaffected.

—The rights of the surety to retain and reimburse himself from funds that have been left with him for indemnity by the bankrupt principal are unaffected where the indemnity was given at the time of becoming surety.⁶

§ 1515. No Duty on Creditor to Prove Claim against Bankrupt Principal.—It is not incumbent upon the creditor to take any steps to prove the claim, where, at any rate, the surety does not demand it; nor to notify the surety or endorser, nor tender the note, so as to give the latter an opportunity to present it.⁷

§ 1516. Right of Surety or Endorser to Prove Creditor's Claim against Bankrupt Principal.—If the surety or endorser demands of the creditor that he prove the claim, and the creditor fails or refuses to do so, the surety or endorser may prove the claim himself.⁸ He undoubtedly may prove it without demand, provided he is able to attach the written instrument to his proof of claim.

§ 1517. Where Creditor Refuses to Let Surety Have Written Instrument to Attach to Proof, Surety Not Released.—If the creditor himself fails to prove the claim and refuses to permit the surety to have the written instrument to file with the proof of claim as required by statute, the surety is nevertheless not released. His remedy is to pay the debt.⁹

§ 1518. Unless Surety Offers to Indemnify Creditor against Expense.—But, if the surety should offer to indemnify the creditor against expense and the creditor should still refuse, then, doubtless, the surety would be released, at least to the extent of dividends lost.¹⁰

6. Compare, *In re Franklin*, 6 A. B. R. 285, 106 Fed. 666 (D. C. Mass., affirmed by Sup. Ct. U. S. in *Jacquith v. Rowley*, 9 A. B. R. 525, 188 U. S. 620). *Obiter*, *In re Eastern Commission & Importing Co.*, 12 A. B. R. 305, 129 Fed. 847 (D. C. Mass.).

7. *Bank v. Sawyer*, 6 A. B. R. 154 (Sup. Jud. Ct. Mass.).

8. Bankr. Act, § 57 (i). See ante, §§ 611, 642, 645.

9. Compare *Bank v. Sawyer*, 6 A. B. R. 154 (Sup. Jud. Ct. Mass.).

10. *Obiter*, *Bank v. Sawyer*, 6 A. B. R. 154 (Sup. Jud. Ct. Mass.).

§ 1519. Creditor Entitled to Prove against Both Principal and Surety Where Both Bankrupt.—A creditor may prove the full amount of his note or other commercial paper against both maker and endorser where both are in bankruptcy, and may collect from both estates dividends until his whole debt is satisfied.¹¹

Board of Commrs. Kan. *v.* Hurley, 22 A. B. R. 209, 169 Fed. 92 (C. C. A. Kan.): "The obligee in a bond, or the holder of a claim upon which several parties are personally liable, may prove his claim against each of the estates of those who become bankrupt, and may at the same time pursue the others at law, and he may recover notwithstanding payments after the bankruptcy by other obligors or by their estates dividends from each estate in bankruptcy upon the full amount of his claim at the time the petition in bankruptcy was filed therein, until from all sources he has received full payment of his claim, but no longer. The filing of a petition in bankruptcy vests in each creditor of the bankrupt an equitable estate in such a proportion of his property as the creditor's claim bears to the entire amount of the provable claims."

§ 1520. But Bankrupt Estate Not to Pay Two Dividends on Same Claim.—But a sound and well-established rule applicable to the settlement of insolvent estates is that the estate must never pay two dividends with respect to the same claim.¹²

First Nat'l Bk. *v.* Eason, 17 A. B. R. 593, 149 Fed. 204 (C. C. A. Tex.): "The appellant has two obligations of the bankrupt, one is on a note of \$15,000 of which the bankrupt was maker, the other is on an indorsement on a forged note for \$15,000, given as collateral to secure the first-mentioned note. The appellant seeks to prove both obligations against the bankrupt's estate. There was only one consideration, really only one debt, and the appellant is entitled to only one satisfaction. The payment of either obligation would extinguish the other. The District Court held that the appellant could not prove both and thus establish a double liability against the bankrupt's estate.

"The decree appealed from is affirmed."

§ 1521. Creditor Receiving Dividends Out of Maker's Estate First, Whether May Prove Only for Unpaid Balance against Surety.—But if the creditor receives dividends out of the maker's estate before he has proved his claim against the endorser, it has been held that he may prove against the endorser merely for the unpaid balance.¹³ Yet this would not be the rule except in cases where such dividends out of the maker's estate were received before the filing of the surety's bankruptcy petition.

Board of Commrs. Kans. *v.* Hurley, 22 A. B. R. 209, 169 Fed. 92 (C. C. A. Kans.): "A single question remains: Is the claim of a creditor against the estate of a surety in bankruptcy upon which the principal has made partial

11. In re Swift, 5 A. B. R. 415, 106 Fed. 65 (D. C. Mass.). But compare, In re Martin, 5 A. B. R. 424, 105 Fed. 753 (D. C. N. Y.).

12. (1841) In re Sterling, Ahrens &

Co., 1 Fed. 169; Oriental Bank *v.* European Bank, 7 L. R. (Ch. App.) 69.

13. In re Swift, 5 A. B. R. 415, 106 Fed. 65 (D. C. Mass.). Compare, to same general effect, In re Martin, 5 A. B. R. 423, 105 Fed. 753 (D. C. N. Y.).

payments after the date of the filing of the petition in bankruptcy entitled to allowance at and to dividends upon the amount owing upon it when the petition was filed, or upon the amount remaining unpaid upon it when the final allowance of it is made, or when the respective dividends are paid? In the discussion of this question preferences, securities consisting of pledged or mortgaged property, such as are required to be surrendered or applied upon claims by the bankruptcy law, are laid out of consideration, and what is said has no reference to rights under them, because no such rights are in issue here. Laying out of view then such preferences and securities, the status of claims at the time of the filing of the petition in bankruptcy, and not at any subsequent time, fixes the rights of their owners to share in the distribution of the estate of the bankrupt. Bankruptcy Act, § 63 a (1), * * * *Swarts v. Siegel*, 8 Am. B. R. 690, 117 Fed. 13, 15, 54 C. C. A. 399, 401; *In re Bingham* (D. C.), 2 Am. B. R. 223, 94 Fed. 796. On that date the property of the bankrupt passes from his control to the court or to its receiver, and thence to the trustee in trust for the creditors of the bankrupt in proportion to the amounts of their claims at that time. On that date there vests in each creditor as a cestui que trust an equitable estate in such a part of the property of the bankrupt as the amount of his provable claim at that time bears to the entire amount of the provable claims against the estate. * * * The obligee in a bond, or the holder of a claim, upon which several parties are personally liable, may prove his claim against the estates of those who become bankrupt and may at the same time pursue the others at law, and, notwithstanding partial payments after the bankruptcy by other obligors or their estates, he may recover dividends from each estate in bankruptcy upon the full amount of his claim at the time the petition in bankruptcy was filed therein until from all sources he has received full payment of his claim, but no longer. *In re Babcock* (Mr. Justice Story), 2 Fed. Cas. 289, 291 (No. 696); *Ex parte Farnsworth*, 8 Fed. Cas. 1055, 1056 (No. 4,672; *In re Hicks*, 12 Fed. Cas. 113, 114 (No. 6,456); *In re Howard*, 12 Fed. Cas. 625, 627 (No. 6,750); *Downing's Assignee v. Traders' Bank*, 2 Dill. 136, 144, 7 Fed. Cas. 1008, 1011 (No. 4,046); *In re Souther*, 22 Fed. Cas. 815 (No. 13,184)."

§ 1522. Creditor Receiving Dividends Out of Surety's Estate First, Surety Entitled to Subrogation to Creditor's Claim against Maker's Estate in Proportion to Dividend Paid by Surety.—And if the creditor shall have received his dividend on his full claim from the surety's estate first, the surety's estate will be entitled to subrogation to the creditor's claim against the maker to the extent of the dividends paid by the surety's estate.

[1841] *In re Sterling, Ahrens & Co.*, 1 Fed. 169: "It is quite obvious, that if this proof is allowed the Oriental Bank will pay a double dividend on the same debt. It appears to me clearly that it is substantially the same debt, because, if all parties had been solvent, whatever sums the Oriental Bank might have paid to the Agra Bank, although they would have paid it, no doubt, for the purpose of performing the contract they had entered into by their indorsement, yet, substantially, whatever sums they might have paid to the Agra Bank would have gone in reduction of the sum which the Oriental had promised to pay to the European Bank. In that case the Oriental Bank could never have been called upon to pay these bills twice over. It would have made no difference that they had entered into two contracts with the two separate parties that they would pay the bills, namely, with the European Bank as acceptors, and with the Agra Bank as holders. It is clear that they would have performed both contracts by

paying the bills once. * * * It has been the law for a great number of years, with reference to proofs in bankruptcy, that if an acceptor accepts bills for the accommodation of the drawer, and the drawer enters into a contract, express or implied (and I do not think there is any difference between the two), that he will provide for the bills when they become due, and then the drawer becomes bankrupt, there cannot be a double proof against his estate, namely, one proof by the holder of the bill, and the other proof by the acceptor of the bill on the contract of indemnity. * * * The principle itself—that an insolvent estate, whether wound up in chancery or in bankruptcy, ought not to pay two dividends in respect of the same debt—appears to me to be a perfectly sound principle. If it were not so a creditor could always manage, by getting his debtor to enter into several distinct contracts with different people for the same debt, to obtain higher dividends than the other creditors, and perhaps get his debt paid in full. I apprehend that is what the law does not allow; the true principle is that there shall only be one dividend in respect of what is in substance the same debt, although there may be two separate contracts."

§ 1523. Discharge of Bankrupt Principal, Equivalent to Return of Execution Unsatisfied.—Discharge of the bankrupt maker is equivalent to a return of execution wholly or partly unsatisfied, so far as the creditor's rights against the surety are concerned.¹⁴

§ 1524. Staying Discharge and Permitting Creditor to Take Judgment to Fix Liability on Surety.—It is proper for the bankruptcy court to stay proceedings for a discharge and to refuse to stay proceedings against the bankrupt, in order to permit a qualified judgment to be taken, where the obtaining of such a judgment or the taking of other steps is necessary in order to perfect the creditor's rights against a third party, surety or guarantor.¹⁵

In re Mercedes Import Co., 21 A. B. R. 590, 166 Fed. 427 (C. C. A. N. Y.), reversing 20 A. B. R. 648: "The district judge was not obliged to grant the stay under § 11 of the Bankruptcy Act, but did so because he thought that the creditor had no better equity against the surety than he had against the bankrupt. As the trustee in bankruptcy has no interest whatever in the claim against the surety we think the creditor's rights and equities are questions to be disposed of by the State court. * * * We think the court in which the action is pending should be left free to take whatever steps it thinks equitable in the premises in accordance with its own practice, and the order granting the stay is therefore reversed."

¹⁴. In re Martin, 5 A. B. R. 423, 105 Fed. 753 (D. C. N. Y.).

¹⁵. In re Marshall Paper Co., 2 A. B. R. 633 (D. C. Mass.), reversed, on other grounds, in 4 A. B. R. 468, 102 Fed. 872. See note to Continental Nat. Bk. v. Katz, 1 A. B. R. 21 (Super. Ct. Ill.). Compare, analogously, as to realizing on liens notwithstanding discharge, Powers Dry Goods Co. v. Nelson, 7 A. B. R. 506, 10 N. Dak. 580. King v. Block Amusement Co., 20 A. B. R. 784, 126 App. Div. 48, 111 N. Y. Supp. 102, quoted at § 1447; In re Maher, 22 A. B. R. 290, 169 Fed. 997 (D. C. Ga.);

rule affirmed but not applied because indemnity given, In re Maaget, 23 A. B. R. 14, 173 Fed. 232 (D. C. N. Y.); In re Ennis & Stoppani, 22 A. B. R. 679, 171 Fed. 755 (D. C. N. Y.), quoted post, this same section; obiter (creditor seeking to subject property not exempt as to him without staying discharge), Bowen & Thomas v. Keller, 22 A. B. R. 727, 130 Ga. 31. Also, see §§ 648, 1914, 2200, 2446, 2712. And the same rule would prevail as to exempt property. See § 1102, et seq. Compare, ante, § 234, note.

In *re Remington Auto & Motor Co.*, 9 A. B. R. 533, 119 Fed. 441 (D. C. N. Y.): "Some of the creditors of this alleged bankrupt corporation are now seeking to put their respective claims in judgment, issue execution, and thus place themselves in a position to bring an action in equity of the nature and for the purpose mentioned. If this preliminary action be necessary when bankruptcy has intervened, the injunction should not be made permanent or continued; for, if such a liability exists, and it can be enforced only by a creditor with judgment and execution returned unsatisfied, or by the trustee, when appointed, after a creditor or creditors have put themselves in this position, then to grant or make permanent this injunction will be to deprive the creditors of their rights. Is this liability an asset of the corporation, and, if so, will it pass to the trustee when appointed, and may he enforce it for the benefit of all? Will the proof of the insolvency of the corporation and the adjudication of its bankruptcy, followed by the proof in due course of the claims of creditors, be a substitute for judgment against the corporation and execution returned unsatisfied? If so, then action by creditors against the stockholders of the corporation may be unnecessary. But suppose the trustee, when appointed, should refuse to bring the action, must the creditors lose their rights to proceed against the stockholders which they might, should they be denied the right to put their claims against the corporation into judgment? * * * So long as uncertainty exists as to the effect of enjoining these creditors from prosecuting their claims against this corporation to judgment, the wise course is to permit the creditors to bring their actions and prosecute them to judgment; otherwise the creditors may be deprived of a valuable part of the assets of the corporation."

Obiter, In *re Eastern Commission & Importing Co.*, 12 A. B. R. 305, 129 Fed. 847 (D. C. Mass.): "Again, if after adjudication he were seeking to proceed with his suit in order to obtain a special judgment * * * this court might refuse to exercise its discretion to stay him."

Bank v. Elliott, 6 A. B. R. 415, 85 N. W. (Wis.) 417: "It is conceded that if a defendant is discharged in bankruptcy from a debt, pending proceedings to enforce it, he is entitled to plead such circumstances in bar of further proceedings for personal judgment, if the plaintiff does not voluntarily discontinue the action, and to recover on such plea. But it is said that if an action is wholly in rem, or partly in rem and partly in personam, its status as an action to reach the res is not disturbed by a discharge of the defendant in bankruptcy, if the plaintiff's interest therein be preserved by the Bankruptcy Act. The authorities seem to be uniform to that effect. *Roberts v. Wood*, 38 Wis. 60; *Bates v. Tappan*, 99 Mass. 376; *Bowman v. Harding*, 56 Me. 559; *Leighton v. Kelsey*, 57 Me. 85; *Ingraham v. Phillips*, 1 Day, 117; *Jones v. Lellyett*, 39 Ga. 64; *Pierce v. Wilcox*, 40 Ind. 70; *Stoddard v. Locke*, 43 Vt. 574; *May v. Courtney*, 47 Ala. 185; *Kittredge v. Warren*, 14 N. H. 509; *Munson v. Railroad Co.*, 120 Mass. 81.

"In *Bowman v. Harding*, it was insisted on behalf of the discharged party that he was, by the express terms of the Bankruptcy Act, released from all his debts, and that no such discharged debt could, by implication, be considered to have sufficient life to form the basis of a judgment even in form against him. The court thought otherwise, reasoning that the language of the Bankruptcy Act, preserving a lien incident to a debt, by implication preserved the debt, notwithstanding its discharge, so far as necessary to make the lien effective. Treating of the same subject, in *Leighton v. Kelly*, supra, the court said, in substance, the provisions of the Bankruptcy Act are not to be construed so as to preclude the rendition of such a judgment as is necessary to enable a lien claimant, whose interest in property is preserved to him by the act, to perfect and realize upon it. In *Bates v. Tappan* this language was used:

"The provisions for a full discharge * * * must be construed, as they well may be, so as not to prevent the enforcement of a lien, which the statute itself permits, by any requisite proceedings therefor which do not involve a judgment in personam. A lien by attachment can be enforced in no other ways than by the qualified judgment which was rendered in the Superior Court, and it must therefore be affirmed."

"The present Bankruptcy Act has the same features as the Act of 1867, which were the foundation of the adjudications cited. It provides that 'All levies, judgments, attachments, or other liens, obtained through legal proceedings against a person who is insolvent, at any time within four months prior to the filing of a petition in bankruptcy against him, shall be deemed null and void in case he is adjudged a bankrupt,' etc. Section 67f. The language as clearly, by implication, preserves all liens claimed in legal proceedings, of sufficient age to be outside the four months limit, as it expressly annuls those within such limit. The preservation of certain liens necessarily left the lien claimants free to pursue the necessary legal or equitable remedies to render them effective."

Provided such third party by becoming such surety had not released property of the bankrupt from an attachment, execution or other sequestration by legal proceedings itself annulled by the bankruptcy.¹⁶

Hill v. Harding, 130 U. S. 699: "If an attachment of property in an action in a State court is dissolved by the defendant's entering into a recognizance, with sureties, to pay, within 90 days after any final judgment against him, the amount of that judgment and the defendant, after verdict against him, obtains his discharge in bankruptcy upon proceedings commenced more than four months after the attachment, the Bankrupt Act does not prevent the State court from rendering judgment against him on the verdict, with a perpetual stay of execution, so as to have the plaintiff at liberty to proceed against the sureties. Such attachment being recognized as valid by the Bankruptcy Act (Rev. St., § 5044), a discharge in bankruptcy does not prevent the attaching creditors from taking judgment against the debtor in such limited form as may enable them to reap the benefit of their attachment. When the attachment remains in force, the creditors, notwithstanding the discharge, may have judgment, against the bankrupt, to be levied only upon the property attached. *Peck v. Jenness*, 7 How. 612, 623; *Doe v. Childress*, 21 Wall. 642. When the attachment has been dissolved, in accordance with the statutes of the State, by the defendant's entering into a bond or recognizance, with sureties, conditional to pay to the plaintiffs, within a certain number of days after any judgment rendered against him on a final trial, the amount of that judgment, the question whether the State court is powerless to render even a formal judgment against him for the single purpose of charging such sureties, * * * depends upon the extent of the authority of the State court under the local law."

In *re Ennis & Stoppani*, 22 A. B. R. 679, 171 Fed. 755 (D. C. N. Y.): "Though I cannot wholly vacate the stay, I can, however, permit the petitioner to enter his judgment against the bankrupt, and to do so much else as may be necessary to perfect any rights he may have under the undertaking, if any. The undertak-

16. Inferentially and obiter, In *re Eastern Commission & Importing Co.*, 12 A. B. R. 305, 129 Fed. 847 (D. C. Mass.); inferentially, obiter, *Klipstein v. Allen-Miles*, 14 A. B. R. 15, 136 Fed. 385 (C. C. A. Ga.); analogously, In *re Franklin*, 6 A. B. R. 285, 106 Fed. 666

(D. C. Mass., affirmed sub nom. *Jacquith v. Rowley*, 9 A. B. R. 525, 188 U. S. 620); inferentially, obiter, *Paxton v. Scott*, 10 A. B. R. 81, 92 N. W. 611 (Neb.): "If the creditor have an attachment or other lien he may have a special judgment entered in rem."

ing was taken out more than four months before the petition was filed; and, assuming that the indemnity given the surety created a lien under § 67c or 67f, which it is not necessary to decide, such a lien is not invalid. If the petitioner can enforce the undertaking, I will aid him to do so."

Thus, if the surety were simply a surety on appeal from a judgment in personam, where the judgment did not operate to sequester any property, probably such qualified judgment would be proper, or where, as in *Hill v. Harding* 130 U. S. 699, the attachment lien vacated was good against bankruptcy, having been taken more than four months preceding bankruptcy.

But where the surety has, by becoming surety, released the bankrupt's property from an invalid lien, it would be manifestly improper to aid the creditor in obtaining the money value of that which the Bankruptcy Act forbids him to obtain in specie.¹⁷

And the matter of stay rests in the sound discretion of the court.¹⁸

But stay should not be granted on application of the trustee where assets of the bankrupt estate are not involved nor creditors' rights prejudiced. Thus, where stay of a creditor's suit in personam had been granted on the ground that the bond in attachment had been given to the creditor after the passage of the Bankruptcy Act and that therefore the creditor must be presumed to have taken it with the act in view, the upper court held that the stay was erroneous because it did not concern the trustee what judgment was had to bind the surety.¹⁹

Such staying of discharge and refusal to stay the creditors' proceedings are not a denial of the bankrupt's right to discharge, nor do they in the slightest degree interfere with his obtaining the full benefit of the discharge when subsequently granted. This is so for the reason that the judgment so obtained "after the filing of the petition and before the consideration of his application for discharge" is, by the express words of § 63 (b) (5) a provable debt; and, being a provable debt is, consequently, discharged by the discharge of the bankrupt. Its enforcement against the bankrupt in personam or against his subsequently acquired property may be enjoined precisely as the enforcement of any other provable judgment debt may be enjoined.

But, even though the bankruptcy court should thus stay the discharge

17. Inferentially, *Klipstein v. Allen-Miles*, 14 A. B. R. 15, 136 Fed. 385 (C. C. A. Ga.); inferentially, *In re Eastern Commission & Importing Co.*, 12 A. B. R. 305, 306, 129 Fed. 847 (D. C. Mass.). Analogously, obiter, *King v. Block Amusement Co.*, 20 A. B. R. 48, 111 N. Y. Supp. 102, quoted at § 1447; inferentially, *Crook-Horner Co. v. Gilpin*, 23 A. B. R. 350 (Md. Ct. App.). See analogous subject under the subject of "Exemptions," ante, § 1070 and § 1102. See under subject of "Dis-

charge," post, §§ 2414, 2711, 2712.

18. *In re Mercedes Import Co.*, 21 A. B. R. 590, 166 Fed. 427 (C. C. A. N. Y., reversing 20 A. B. R. 648, on other grounds); *In re Mercedes Import Co.*, 20 A. B. R. 648, 166 Fed. 427, reversed, on other grounds, in 21 A. B. R. 590, 166 Fed. 427.

19. *In re Mercedes Import Co.*, 21 A. B. R. 590, 166 Fed. 427 (C. C. A. N. Y., reversing 20 A. B. R. 648), quoted supra.

in order to permit a qualified judgment to be taken with perpetual stay of execution thereafter, the question might still remain as to whether the policy of the State law would permit the State court to render such qualified judgment.²⁰

²⁰. Compare, *Crook-Horner Co. v. Kendrick & Roberts v. Warren Bros., Gilpin*, 23 A. B. R. 350 (Md. Ct. App.); 110 Md. 47, 72 Md. 461.

PART V.

DISCOVERING, COLLECTING AND SEPARATING ASSETS.

CHAPTER XXXI.

DISCOVERING ASSETS; GENERAL EXAMINATIONS OF BANKRUPTS AND WITNESSES.

Synopsis of Chapter.

- § 1525. General Examinations of Bankrupts and Witnesses.
- § 1526. Analogous to Examinations of Insolvent Debtors Elsewhere.
- § 1527. Who May Be Examined—"Any Designated Person" Including Bankrupt and Wife.
- § 1528. Examination of Each Witness a Separate Proceeding.
- § 1529. At Whose Instance Examination to Be Had.
- § 1530. One General Examination of Bankrupt a Matter of Absolute Right.
- § 1531. But Examination of Other Persons Not.
- § 1532. Creditor before Filing Claim May Examine, but Proof May Be Required.
- § 1533. Application for Examination—Notice Not Required.
- § 1534. Notice to Witness Proper, Where Second Examination Sought.
- § 1535. Notice to Creditors of Examination of Bankrupt Requisite.
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- § 1537. Order for Examination to Be Entered and Served.
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- § 1542. Bankrupt Examined at Any Time after Adjudication, Even after Discharge.
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- § 1551. But Examiner Must Develop Facts Showing Sufficient Connection with Bankrupt to Make Further Inquiry Relevant.
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- § 1554. Referee to Rule on Admissibility and to Exclude Incompetent Testimony.
- § 1555. General Examination Competent as Admission in Subsequent Litigation against Same Party.
- § 1555½. But Not to Be Considered Unless Actually Introduced or Stipulated in.
- § 1556. Bankrupt's Testimony Not to Be Used in Criminal Proceedings against Him.
- § 1556½. But Such Immunity Is Not a Bar to Prosecution for Perjury Committed by Bankrupt When Examined under § 7 (9).

- § 1557. Whether Protection Applies Only to Federal Prosecution.
- § 1558. Incriminating Questions—Constitutional Rights Preserved, Notwithstanding § 7 (9).
- § 1559. Where Answer by No Reasonable Possibility Could Tend to Incriminate, No Privilege.
- § 1560. Privilege Does Not Authorize Refusal to Be Sworn Altogether nor to Produce Documents nor to File Schedules.
- § 1561. Privilege to Be Claimed at Time Question Asked or Production Demanded.
- § 1562. Privilege Not Waived by Voluntary Bankruptcy.
- § 1562½. Conditional Waiver of Privilege.
- § 1563. Pendency of Litigation with Witness, No Excuse for Refusing to Testify.
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- § 1565. Privileged Communications Respected.
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- § 1567. Competency of Witnesses Governed by What Law.
- § 1568. Contempt for "Willfully Evasive" or "Flagrantly False" Testimony.
- § 1568½. Attendance of Bankrupts or Witnesses Confined as Prisoners or in Institutions.
- § 1569. Attendance of Witnesses Residing Out of State or Farther than One Hundred Miles.
- § 1570. General Examination of Nonresident Bankrupt or Witness before Another Referee, or State Judge.
- § 1571. Order for Examination in Another District, Whether Ancillary Proceedings Requisite.
- § 1572. Method Where before Judge of State Court or Another Referee.
- § 1572½. Depositions.
- § 1573. Witness, as Such, Not Entitled to Attorney.
- § 1574. But Is Entitled if Witness Be Creditor or Bankrupt.
- § 1575. Witness' Fees and Mileage.
- § 1576. Contempt for Disobedience of Subpœna.
- § 1577. No Witness' Fees to Bankrupt, but Expenses, Where Examined Away from His Town.
- § 1578. Bankrupt Voluntarily Removing Residence after Adjudication Not Entitled to Reimbursement.
- § 1579. Employment of Stenographer.

§ 1525. **General Examinations of Bankrupts and Witnesses.**—A court of bankruptcy may, upon application of any officer, bankrupt or creditor, by order require any designated person, including the bankrupt and his wife, to appear in court or before the referee, or the judge of any state court, to be examined concerning the acts, conduct or property of a bankrupt whose estate is in process of administration under the act, provided that the wife may be examined only touching business transacted by her or to which she is a party and to determine the facts whether she has transacted or been a party to any business of the bankrupt.¹

And it is made one of the statutory duties of the bankrupt, when present

¹. Bankr. Act, § 21 (a). In re Bryant, 26 A. B. R. 504, 188 Fed. 530 (D. C. Pa.).

at the first meeting of his creditors, and at such other times as the court shall order, to submit to an examination concerning the conducting of his business, the cause of his bankruptcy, his dealings with his creditors and other persons, the amount, kind and whereabouts of his property, and, in addition, all matters which may affect the administration and settlement of his estate.²

§ 1526. Analogous to Examinations of Insolvent Debtors Elsewhere.—The bankruptcy law furnishes a most searching and summary method for the discovery of hidden assets, by means of the examination of the bankrupt and other witnesses, and this examination is in practice much used and has always been a feature of bankruptcy jurisprudence from the earliest statute of King Henry VIII down to the present time.³

It is true that similar provisions are to be found in other branches of jurisprudence taken up with the affairs of insolvent debtors, as, for instance, the examination of the debtor in assignment or insolvency proceedings.

Boyd v. Glucklich, 8 A. B. R. 403, 116 Fed. 131 (C. C. A. Iowa): "In some of the States there are laws providing for the examination of debtors under oath for the purpose of discovering what, if any, property they have applicable to the payment of their debts. The proceeding is analogous in all respects to the examination of the bankrupt under the Bankrupt Act."

Nevertheless, it is found in practice that, so far, at any rate, as concerns assignment proceedings, the examination of the debtor, the assignor, does not approach in its keenness the examination of the debtor which is had in bankruptcy. Perhaps the reason for this is not hard to find. In assignment proceedings the creditors have, in fact (whatever be the theory), no common agent to do the examining for them as they have in bankruptcy, and of course no one creditor cares to assume the responsibility and expense of such an examination alone when he himself will reap only a pro rata share of the benefits resulting from the discovery of any hidden assets. To be sure, in theory, assignment laws afford quite as ample opportunity for such examination as does the bankruptcy law and they also supply an officer to make the examination; but that officer is the assignee himself, who owes his office to the favor of the debtor, and most commonly is a personal friend or even the attorney of the assignor, and consequently is more interested in befriending the assignor than in exposing property concealed by him. It is not, then, a matter of surprise that an examination of the assignor under such circumstances would be likely to be lukewarm.

In bankruptcy proceedings, on the other hand, the examination of the bankrupt follows almost as a matter of course, and being conducted by the

² Bankr. Act, § 7 (9). In re *Walter W. Chamberlain*, 25 A. B. R. 37, 180 Fed. 304 (D. C. N. Y.).

³ See introd., § (g), page 6.

trustee elected by the creditors and responsible to them, is most searching and inquisitorial in its character.

In *re Bryant*, 26 A. B. R. 504, 188 Fed. 530 (D. C. Pa.): "The vigorous and skillful use of examination of insolvent bankrupts is often the only means by which creditors are enabled to prevent the bankruptcy act being turned into a shield for dishonesty. If hardship and inconvenience result from such examinations, as they sometimes may, it should be remembered that a discharge of the bankrupt from his debts is a great privilege and a prize that will reward the honest debtor amply for such inconvenience."

§ 1527. Who May Be Examined—"Any Designated Person" Including Bankrupt and Wife.—Any designated person may be examined; including the bankrupt and his wife.⁴ Thus, a trustee or assignee in insolvency may be examined.⁵ Likewise, the officers of a corporation in which the bankrupt was a stockholder or otherwise interested, may be examined and be required to produce corporate books for inspection.⁶ The bankrupt, of course, may be examined.⁷ And the officers and members of corporations are for certain purposes "the bankrupts" in cases of bankrupt corporations,⁸ but of course not so as to entitle them to all the privileges, or subject them to all the liabilities of bankrupts. And it is even a question whether such officers, when examined, are not entitled to witness fees, as any other witness. The bankrupt's wife may be examined.⁹

§ 1528. Examination of Each Witness a Separate Proceeding.—These general examinations of different witnesses are not all one proceedings, and need not be adjourned from day to day until examination of all the witnesses is finished. Each witness' examination is a separate and independent matter, and when it is concluded there need be no adjournment for other witnesses. Witnesses may be examined independently, and in fact their examinations are wholly independent.¹⁰

§ 1529. At Whose Instance Examination to Be Had.—The examination may be had at the instance of the trustee, receiver, or any other officer, or of any creditor, or of the bankrupt¹¹ himself. Thus, it may be

4. Bankr. Act, § 21 (a).

5. In *re Pursell*, 8 A. B. R. 96, 114 Fed. 371 (D. C. Conn.).

6. In *re Fixen & Co.*, 2 A. B. R. 822, 96 Fed. 748 (D. C. Calif.); In *re Horgan & Slattery*, 3 A. B. R. 253, 257, 98 Fed. 414 (C. C. A. N. Y.).

7. Bankr. Act, §§ 21 (a), 7 (9).

In *re Fellerman*, 17 A. B. R. 790, 149 Fed. 244 (D. C. N. Y.): " * * * and when examined at the first meeting of the creditors it was the duty of each of them (§ 7, subsec. 9) to submit to an examination concerning 'his dealings with his creditors and other persons,' and in respect of 'all matters which may affect the administration and settlement of his estate,' and the

obligation to submit to the examination involved the duty of answering truthfully and as intelligently, connectedly and fully as mental equipment would permit."

8. *Alphin & Lake Cotton Co.*, 12 A. B. R. 653, 131 Fed. 824 (D. C. Ark.). Impliedly, In *re Horgan & Slattery*, 3 A. B. R. 253, 257, 98 Fed. 414 (C. C. A. N. Y.).

9. See post, § 1565, et seq.

10. Compare, inferentially, In *re Cobb*, 7 A. B. R. 104 (Ref. Mass.).

11. **Dismissal of Discharge Petition for Failure to Have First Meeting Called.**—The failure to call the first meeting of creditors, so as to afford an opportunity for examination of the

had at the instance of the receiver;¹² likewise, at the instance of the trustee, or creditors.¹³

Ordinarily the trustee makes the application; but, in case he refuses to do so, the creditor may apply for an order directing the trustee to examine, or permitting the creditor himself to examine,¹⁴ at the expense of the estate.

§ 1530. One General Examination of Bankrupt a Matter of Absolute Right.—It is an absolute right, of which creditors may not be deprived, to have at some time and place an opportunity to examine the bankrupt.

§ 1531. But Examination of Other Persons Not.—But it is not an absolute and unqualified right that a creditor has to demand the issuance of a summons for the general examination of a third person: it lies within the discretion of the court.

In *re Andrews*, 12 A. B. R. 267, 130 Fed. 383 (D. C. Mass.): In this case a summons for the examination of the bankrupt's former assignee for creditors was asked for by a creditor, but was refused by the referee, for reasons not stated in the opinion of the reviewing court, and the refusal was sustained, the reviewing court presuming that the examination was being asked for in another interest than that of the estate. The Court said:

"This provision is not intended to give the creditor an unqualified right to demand the issuance of the summons. Ordinarily, the examination is made by the trustee, and after his appointment a creditor should ordinarily apply to him. If the trustee refuses to undertake the examination, the creditor may apply to the court for an order directing him to do so. To order the trustee to examine is manifestly a matter of discretion. Doubtless the creditor may apply to the court in order to carry on the examination himself, but the court is not wholly without discretion to refuse the application."

bankrupt is by rule held in the Southern and Eastern Districts of New York sufficient cause for dismissing the discharge. And it has been held that such dismissal is not obnoxious to the bankruptcy act. In *re Wollowitz*, 27 A. B. R. 558, 192 Fed. 105 (C. C. A. N. Y.). See also, § 2480. The bankruptcy rule 20 of the Southern District of New York provides as follows: "If the first meeting of creditors is not called and the examination of the bankrupt at such meeting begun, carried on and completed before the discharge is filed, the referee is directed to certify such facts to the court, and thereupon, upon notice to the bankrupt, an application to dismiss the petition for discharge may be made." This rule was necessitated by the rule, since modified, permitting the referee to refuse to call the first meeting of creditors until indemnified therefor. The result of this latter rule was that, the bank-

rupt not having any money and creditors not being willing to spend any more money, frequently no first meeting was called for months. The subsequent modification of the indemnity rule has obviated the need of the dismissal rule. The dismissal rule still prevails, however, in the Eastern District of New York.

12. In *re Fixen & Co.*, 2 A. B. R. 822, 96 Fed. 748 (D. C. Calif.); In *re Fleischer*, 18 A. B. R. 194, 151 Fed. 81 (D. C. N. Y.).

13. In *re Andrews*, 12 A. B. R. 267, 130 Fed. 383 (D. C. Mass.); impliedly, In *re Walker*, 3 A. B. R. 34, 96 Fed. 550 (D. C. S. Dak.); impliedly, In *re Jehu*, 2 A. B. R. 498, 94 Fed. 638 (D. C. Iowa).

14. In *re Andrews*, 12 A. B. R. 267, 130 Fed. 383 (D. C. Mass.): Compare similar rule as to other action in behalf of creditors, post, § 824.

And cause should be shown; but the sufficiency of grounds rests within the discretion of the court, the court including the referee.

In *re Abbey Press*, 13 A. B. R. 17, 134 Fed. 51 (C. C. A. N. Y.): "Any order for examination of any witness other than the bankrupt, whether on a first or second examination, should be for a special cause shown, but the authorities cited show that it has been uniformly held that it is within the discretion of the referee to decide in each particular case what cause is sufficient and upon what information he will make the order."

§ 1532. Creditor before Filing Claim May Examine, but Proof May Be Required.—A creditor who has not filed his claim nor had the same allowed, may examine the bankrupt and witnesses, even though he may not be entitled to vote for trustee, share in dividends or otherwise participate in creditors' meetings until his claim has been allowed.¹⁵ But the referee may require proof that he is a creditor.

In *re Walker*, 3 A. B. R. 35, 96 Fed. 550 (D. C. N. Dak.): "The question raised before the referee depends upon the meaning of the term 'creditor,' as employed in these sections. By § 1 of the act it is provided that, unless the same be inconsistent with the context, the word 'creditor' shall be construed to include 'anyone who owns a demand or claim provable in bankruptcy.' There is nothing in the context which requires a restricted meaning of the term as employed in the sections above quoted. Throughout the act, whenever the word is used in a narrow sense, apt language is employed to indicate such an intention. For example, only those whose claims have been allowed are permitted to vote for the trustee (§ 56), or share in the dividends (§ 65), or determine whether a composition shall be accepted (§ 12b). These are some of the cases in which the context shows that the term 'creditor' is used in a narrower sense than that indicated by the definition in § 1, and, when no such restriction is declared by the context, the general terms of the definition must be held to apply. * * * If he is entitled to oppose the discharge without proving his claim, he ought likewise to be allowed to examine the bankrupt for the purpose of establishing the grounds of his objections; and it has been expressly decided that a creditor is entitled to make such examination without first filing specifications of his objections to the discharge. In *re Price*, 91 Fed. 635. [1 A. B. R. 419.] The general principle to be deduced from the entire act would seem to be that only those creditors whose claims have been proved and allowed can participate either in the management of the estate or in the dividends derived therefrom, but as to all other matters any person having a provable claim is entitled to be heard."

In *re Jehu*, 2 A. B. R. 498, 94 Fed. 638 (D. C. Iowa): "I know of no provision of the Bankrupt Act which requires that a creditor must file and prove up his claim before he is entitled to an order for the examination of the bankrupt. Before granting an order for the examination of a bankrupt, the referee should be satisfied that the party applying for the order is in fact a creditor of the bankrupt; but, if this fact be shown, no good reason exists why the examination should not be had, even though the creditor may not have proved his claim in set form."

¹⁵ In *re Rose*, 19 A. B. R. 169 (D. C. Pa.); *obiter*, In *re Samuelsohn*, 23 A. B. R. 528, 174 Fed. 911 (D. C. N. Y.).

To this end he may probably require the creditor to prove his claim in the usual manner of such proof in bankruptcy. But the referee need not require such method. And it has been held, in some cases, that the fact that the bankrupt included the person in his schedules is sufficient proof.¹⁶

In *re Walker*, 3 A. B. R. 35, 96 Fed. 550 (D. C. N. Dak.): "Was there sufficient evidence before the referee to show that the creditor has a provable claim against the estate? I think there was. The claim was listed by the bankrupt as a debt which he was owing, and he was required by § 7 of the act to state under oath the amount of the claim, and the consideration out of which it arose. This, of course, would not establish the claim, nor the right of the creditor to share in dividends; but as to such matters as the examination of the bankrupt, and as against him, it certainly makes out at least a *prima facie* case that the claim exists and is provable against the estate."

And *a fortiori*, a creditor who has not proved his claim may examine the testimony already taken and written out on general examination, and may even require it to be filed with the referee.¹⁷

In *re Kuffler*, 18 A. B. R. 587, 153 Fed. 667, 155 Fed. 1018 (D. C. N. Y.): "These cases all support the view that under the circumstances a person listed as a creditor in the bankrupt's schedules is within the meaning of §§ 1, 21a, and 55b of the bankruptcy law. If an outsider should appear at any time in bankruptcy proceedings and demand the right to examine the bankrupt, for the purpose of obtaining evidence, in order to make up his mind whether he should claim to be a creditor, the situation would be entirely different. But when, as in the present case, a person listed as a creditor states that he has a claim against the bankrupt's estate, and demands an examination in order to decide whether he will take an affirmative part in the bankruptcy proceedings, it would seem that the court has power to let him do so. This will not in any way abrogate the rule in this district, which is entirely proper for general purposes, and the permission granted the creditor upon this motion will not free him from any responsibilities or obligations to meet the pecuniary expenses of the examination he desires."

And thus it has been held that a scheduled creditor, though his claim be barred by the statute of limitations, may examine.

In *re Kuffler*, 18 A. B. R. 587, 153 Fed. 667, 155 Fed. 1018 (D. C. N. Y.): "The statute of limitations is a defense, and not a part of the affirmative claim; and it has been held in a number of cases that a debt may be provable, even where the defense of the statute of limitations is good as against an action brought in the State courts of the State in which the bankruptcy proceeding has been instituted. In *re Ray*, 1 N. B. R. 203, Fed. Cas. No. 11,589; In *re Shepard*, 1 N. B. R. 439, Fed. Cas. No. 12,753. Such debts, therefore, being provable and covered by a discharge, it would seem that all the more a creditor included in the schedules, whose identity is established satisfactorily to the referee, is entitled to be given an opportunity to ascertain the exact condition of the bankrupt's estate before he determines whether it is worth his while to become a

¹⁶ See ante, § 580. In *re Jehu*, 2 A. B. R. 498, 94 Fed. 638 (D. C. Iowa); In *re Rose*, 19 A. B. R. 169 (D. C. Pa.).

¹⁷ In *re Samuelsohn*, 23 A. B. R. 528, 174 Fed. 911 (D. C. N. Y.), quoted at § 915.

party to the proceeding and attempt to obtain a portion of whatever dividend may be declared."

§ 1533. Application for Examination—Notice Not Required.—The application for an order for the examination should be to the court of bankruptcy, that is to say, in practice, to the referee. It need not be in writing and no particular form is necessary. No notice need be given to the witness sought to be examined, if it is his first examination; no cause need be given where it is the bankrupt whose examination is sought,¹⁸ although cause should be shown for the examination of other witnesses; no divulging of the questions to be propounded need be made; and neither the bankrupt nor other witness will be heard upon the propriety of issuing such order.¹⁹

In *re Howard*, 2 A. B. R. 585, 95 Fed. 415 (D. C. Calif.): "The order requiring Hyde to appear as a witness, and be examined concerning the acts, conduct, and property of the bankrupt, was valid, although there was no formal application therefor, showing what questions were proposed to be asked upon such examination, or the particular facts in relation to which he was to be examined. The statute does not contemplate that any such showing shall be made as the basis for an order of this character. The simple application or demand for such an order by any of the persons named in § 21 of the Bankruptcy Law is all that is required to support it."

In *re Abbey Press*, 13 A. B. R. 11, 134 Fed. 51 (C. C. A. N. Y.): "Under the corresponding sections of the Act of 1867, it was held, that the register had jurisdiction to make such orders for the examination of witnesses, In *re Pioneer Paper Co.*, 7 N. B. R. 250, Fed. Cas. No. 11,178, and that it was discretionary with the register to require a written application or to grant such order on a verbal one; and such appears to us to be the proper construction of the present law and to have been the general practice under it. In *re Pioneer Paper Co.*, *supra*; In *re Solis*, 4 N. B. R. 68, Fed. Cas. No. 13,165; In *re Vetterlein*, 4 N. B. R. 599, Fed. Cas. No. 16,926."

§ 1534. Notice to Witness Proper, Where Second Examination Sought.—But if the witness has already been subjected to one full examination in the same proceedings the better practice would require notice to him of the second application, that he be given opportunity to object to another examination; and good cause should be shown by the applicant why the witness should be re-examined; but such notice, even under such circumstances, is not mandatory nor jurisdictional,²⁰ and perhaps is not usually given.

§ 1535. Notice to Creditors of Examination of Bankrupt Requisite.—Ten days' notice by mail to all creditors must be given of every examination of the bankrupt himself.²¹

¹⁸. In *re Bryant*, 26 A. B. R. 504, 188 Fed. 530 (D. C. Pa.), quoted on other points at §§ 1526, 1540.

¹⁹. In *re Cobb*, 7 A. B. R. 104 (Ref. Mass., affirmed by D. C.). To same general effect, In *re Fixen & Co.*, 2 A. B. R. 822, 96 Fed. 748 (D. C. Calif.).

²⁰. Impliedly, In *re The Abbey Press*, 13 A. B. R. 11, 134 Fed. 51 (C. C. A. N. Y.).

²¹. Bankr. Act, § 58 (a): "Creditors shall have at least ten days' notice by mail, to their respective addresses as they appear in the list of the bankrupt

§ 1536. None to Creditors nor Bankrupt for Examination of Other Witnesses.—No notice to creditors is necessary of the examination of other witnesses than the bankrupt; for no provision requiring notices in such cases is found in the statute, the orders in bankruptcy or the prescribed forms.

In *re Cobb*, 7 A. B. R. 104, 106 (Ref. Mass.): "Under the present act no notice is required to be given of the examination of a witness by the trustee under § 21a, and there seems to be no better reason for giving notice to the bankrupt under that section than there was under § 26 of the earlier act. There might indeed be very good reasons why the trustee should wish to pursue his investigations without the bankrupt's knowledge, and as it is the bankrupt's duty to give his trustee all the information and assistance in his power, it would certainly seem incongruous to allow his attorney to appear and cross-examine a witness whom the trustee wishes to examine, when the purpose of cross-examination generally is adverse to the interest of the party by whom the witness is presented."

Nor is notice to the bankrupt of the examination of other witnesses requisite.²²

§ 1537. Order for Examination to Be Entered and Served.—An order must be entered for the examination of each witness.²³

Thereupon a copy of this order, or a subpoena, is issued and served upon the witness. It should properly be under the seal of the court.²⁴

§ 1538. None Requisite for Examination of Bankrupt at First Meeting.—No order is necessary to procure the general examination of the bankrupt himself when he is present at the first meeting of creditors, because the statute itself provides in § 7, clause (9), that the bankrupt shall "submit to examination when present at the first meeting of creditors and

or as afterwards filed with the papers in the case by the creditors, unless they waive notice in writing of (1) All examinations of the bankrupt."

²² In *re Cobb*, 7 A. B. R. 104, 106 (Ref. Mass.).

²³ Form for order: "Upon this _____ day of _____, 191—, upon application of the trustee (or if such be the case, upon application of _____, a creditor), at the hearing whereof no adverse interest was present, it is ordered that John Smith be and he hereby is ordered to appear before the referee in bankruptcy, at his offices, etc., etc., upon the _____ day of _____, 191—, at 10:00 o'clock in the forenoon to be examined concerning the acts, conduct and property of the above named bankrupt, in accordance with law." In *re Fixen & Co.*, 2 A. B. R. 825, 96 Fed. 748 (D. C. Calif.).

²⁴ General Order III: "All process, summons and subpoenas shall issue out

of the court, under the seal thereof, and be tested by the clerks; and blanks, with the signature of the clerk and seal of the court, may, upon application, be furnished to the referees."

Inferentially, In *re Abbey Press*, 13 A. B. R. 13, 134 Fed. 51 (C. C. A. N. Y.): "The subpoena did not bear the seal of the court. The petitioner, however, attended before the referee, and does not seem to have made the objection there. This defect was, therefore, waived by the appearance of the witness without objection on that ground, and, as he was actually before the referee when the order to be sworn was made, the absence of the seal is immaterial." See ante, § 548½.

Inferentially (as to notice upon surety on bond of assignee, where assignee called to accounting), *Cohen v. American Surety Co.*, 22 A. B. R. 909, 132 App. Div. N. Y. 917.

at such other times as the court may order," and the prescribed form of the notice of the first meeting of creditors contains a notification that the bankrupt may be examined at the first meeting.²⁵

§ 1539. But Requisite in Other Cases.—If it is desired to generally examine the bankrupt at any other time than either at the first meeting of creditors or at some adjourned session of the first meeting, an order must be entered and ten days' notice be given to all creditors.²⁶

§ 1540. Second Examination May Be Had.—After the conclusion of one general examination, a subsequent general examination of the bankrupt, or of a witness, may be had.²⁷

In *re Bryant*, 26 A. B. R. 504, 188 Fed. 530 (D. C. Pa.): "Surely the bankrupt should not be unnecessarily harrassed, vexed, or annoyed, but where it appears that the creditors may be benefited by further examination or for any other good reason appearing the order should be allowed."

In *re Mellen*, 3 A. B. R. 226, 97 Fed. 326 (D. C. N. Y.): "But this does not necessarily supersede a further examination of the bankrupt if, on application by objecting creditors, the referee shall deem a further examination reasonable and necessary."

§ 1541. But Good Cause Must Be Shown.—But such subsequent examination, by better practice, is not to be obtained except for good cause and upon notice to him of the application for a second examination.²⁸

However, it is, of course, not necessary to state what is expected to be proved: it is an investigation, not a trial.

In *re Bryant*, 26 A. B. R. 504, 188 Fed. 530 (D. C. Pa.): "Nor was the trustee required to set forth the nature and character of the testimony in detail intended to be adduced. The very purpose of an examination under § 21a is to discover property of the bankrupt or to learn of its whereabouts and as to the acts of the bankrupt with respect thereto. Such an examination is in its very nature an investigation intended to satisfy the minds of those whose judgment it is true is frequently not well founded by which the honest debtor has all to gain."

§ 1542. Bankrupt Examined at Any Time after Adjudication, Even after Discharge.—A bankrupt may be required to attend for examination whenever reasonably required by creditors.²⁹

25. Whether Bankrupt Must Attend Other Meetings unless Ordered.—Nevertheless, apparently, the bankrupt need not attend the first meeting nor any other meeting of creditors unless ordered so to do. See Bankr. Act, § 7 (a) (9).

Obiter, In *re Shanker*, 15 A. B. R. 109, 138 Fed. 863 (D. C. Penn.).

Although he must attend the hearing upon his application for discharge without being ordered so to do: In *re Mellen*, 3 A. B. R. 226, 97 Fed. 326 (D. C. N. Y.); In *re Shanker*, 15 A. B. R. 109, 138 Fed. 862 (D. C. Penn.).

26. In *re Price*, 1 A. B. R. 419, 91

Fed. 635 (D. C. N. Y.). As to orders for examinations of bankrupts or non-resident witnesses before a State Judge or before another referee than the one before whom the case is pending, see post, § 1570.

27. In *re Smelting Co.*, 15 A. B. R. 83, 85, 146 Fed. 336 (D. C. Penn.).

28. In *re Price*, 1 A. B. R. 419, 91 Fed. 635 (D. C. N. Y.). Compare. In *re Abbey Press*, 13 A. B. R. 17, 134 Fed. 51 (C. C. A. N. Y.).

29. In *re Bryant*, 26 A. B. R. 504, 188 Fed. 530 (D. C. Pa.), quoted on other points at §§ 1526, 1540, 1541.

In *re Mellen*, 3 A. B. R. 226, 97 Fed. 326 (D. C. N. Y.): "The correct practice, is to require the bankrupt to attend for examination whenever reasonably required by creditors for the purpose of establishing their objections to his discharge."

He may be examined even after his discharge,³⁰ at any rate to see if he has concealed anything since his discharge.³¹

But there seems no good reason for limiting the right of examination to the discovery of assets concealed since the discharge, nor to restrict it to a period of one year from the discharge. As long as the estate is not closed, the right of general examination exists, subject of course to the right of the bankrupt not to be subjected to unnecessary or repetitious examination.

§ 1543. Bankrupt May Be Put under "General" Examination before Adjudication.—Although there was considerable doubt for some time on the question,³² it has now been definitely settled by the Supreme Court of the United States that the alleged bankrupt may be put under general examination before adjudication.³³

Cameron v. United States, 231 U. S. 710, 31 A. B. R. 604: "This proceeding was prior to the adjudication in bankruptcy, which followed a few days later. Whether the examination of Cameron upon oath at that stage of the proceedings was authorized by the Bankruptcy Act depends upon a construction of clause a, § 21, of the act. The controversy is over the meaning of the phrase, 'a bankrupt whose estate is in process of administration' under this act.' The construction of this provision differs in the federal courts, some of them having held that there can be no such examination until after adjudication, as it is only then that the bankrupt can be subjected to such proceedings. * * * We are of opinion that the estate was in process of administration at the time when the examination before the commissioner was ordered, and the testimony of Cameron given. This court has decided that the filing of the petition in bankruptcy operates to place the property of the alleged bankrupt in custodia legis, and prevents any creditor from attaching it; and, although, by the terms of the Act, the estate does not vest in the trustee at the time of the filing of the petition under the control of the court with a view to its ultimate distribution

30. In *re Westfall Bros. Co.*, 8 A. B. R. 431 (Ref. N. Y.).

31. In *re Peters*, 1 A. B. R. 248 (Ref. Mass.).

32. **Holdings before *Cameron v. United States*, that general examination not available until adjudication.** *Skubinsky v. Bodek*, 22 A. B. R. 689, 172 Fed. 332 (C. C. A. Pa.); In *re Back Bay Auto Co.*, 19 A. B. R. 835, 158 Fed. 679 (D. C. Mass.); *Podolin v. McGettigan*, 29 A. B. R. 406, 193 Fed. 1021 (C. C. A. Pa.); In *re Thompson*, 24 A. B. R. 655, 179 Fed. 874; In *re Davidson*, 19 A. B. R. 833, 158 Fed. 678 (D. C. Mass.); In *re Crenshaw*, 19 A. B. R. 266, 155 Fed. 271 (D. C. Ala.); In *re Herskovitz*, 18 A. B. R. 249, 152 Fed. 316 (D. C. N. Y.); In *re Starke*, 18 A. B. R. 467, 155 Fed. 694 (D. C. N. Y.).

However, it was always conceded that the bankrupt might be examined, under the general powers of the court, as a witness on a motion or other proceedings raising an issue. *Obiter*, In *re Back Bay Auto Co.*, 19 A. B. R. 835, 158, Fed. 679 (D. C. Mass.).

33. **Decisions affirming the right to examination before adjudication, before *Cameron v. United States*.** In *re Fixen & Co.*, 2 A. B. R. 822, 96 Fed. 748 (D. C. Calif.); In *re Fleischer*, 18 A. B. R. 194, 151 Fed. 81 (D. C. N. Y.); *Ex parte Bick*, 19 A. B. R. 68, 155 Fed. 908 (C. C. N. Y.); *Wechsler v. United States*, 19 A. B. R. 1, 158 Fed. 579 (C. C. A. N. Y.); *United States v. Liberman*, 23 A. B. R. 734, 176 Fed. 161 (D. C. N. Y.).

among creditors. *Acme Harvester Co. v. Beekman Lumber Co.*, 222 U. S. 300, 307, 27 A. B. R. 262; and see *Mueller v. Nugent*, 184 U. S. 1, 14, 7 A. B. R. 224, *Everett v. Judson*, 228 U. S. 474, 478, 479, 30 A. B. R. 1, 46 L. R. A. (N. S.) 154. And this is true, notwithstanding, as contended by the petitioner, that should the attempt to obtain an adjudication of bankruptcy fail upon the subsequent hearings, the receivership would necessarily be vacated and the property turned back to the alleged bankrupt.

"In order to arrive at the true meaning of § 21a other provisions as well as the purpose of the Act must be had in view. The object of the examination of the bankrupt and other witnesses to show the condition of the estate is to enable the court to discover its extent and whereabouts, and to come into possession of it, that the rights of creditors may be preserved. If such examination is postponed until after adjudication, which may not take place for at least twenty days, within which the bankrupt in involuntary bankruptcy is given leave to appear and plead, the estate may be concealed and disposed of, and the purpose of the Act to hold it to distribute for the benefit of creditors defeated. The importance of such early examination of bankrupts was emphasized in *Re Fleischer* (D. C. N. Y.), 18 A. B. R. 194, 151 Fed. 81. By subdivision 9 of § 7 of the Act, it is provided that the bankrupt shall, 'when present at the first meeting of his creditors, and at such other times as the court shall order, submit to an examination concerning the conducting of his business, the cause of his bankruptcy, his dealings with his creditors and other persons, the amount, kind, and whereabouts of his property, and, in addition, all matters which may affect the administration and settlement of his estate.'

"Here is found authority to examine the bankrupt at such other times than the first meeting of creditors as the court may direct. This section should be read with § 21a, and throws light upon its proper construction. In this case the petitioner had invoked the jurisdiction of the court, a receiver had been appointed to take possession of the property, the court was so far in possession of it as to prevent other courts from seizing it, and thus defeating the bankruptcy jurisdiction. We are of opinion that the estate was then in process of administration, and the examination ordered was within the jurisdiction of the court."

Under the law of 1841,³⁴ as also under the law of 1867,³⁵ it appears to

34. *Ex parte Lee*, Fed. Cas. 8178 (D. C. N. Y.).

35. In *re Salkey*, 9 Bank. Reg. 107, Fed. Cas. 12,952 (D. C. Ill.): "The question is whether it is competent for District Judge to make an order for examination of a debtor prior to an adjudication. * * * The question arises under the 26th section of the bankrupt law. That section provides that the Court might, on the application of the assignee in bankruptcy, or of any other creditor, at all times require the 'bankrupt' to submit to an examination.

"It is said that the word 'bankrupt' is used here and that there is a distinction made in the bankrupt law subsequent to an adjudication in bankruptcy. * * * It is insisted that the word 'bankrupt' indicates that an examination can not be had until after an adjudication. * * *

"In one sense this is true. He does not necessarily become technically a bankrupt until he is so decided to be by the Court. The argument urged that there should not be this inquisitorial power exercised over the debtor for the purpose of prying into his business affairs, and because the examination might be injurious to his credit by disclosing facts affecting the same, can hardly have much weight when it is recollected that the law provides certain means by which the Court may proceed to determine whether or not the debtor committed an act of bankruptcy. The power of the Court seems to be plenary, prior to the adjudication, not only over the debtor's property, but over his person.

"It might be said with as much reason that the Court should not exercise this power over either his property or his person until it had actually decided

have been possible, upon good cause shown, to obtain an order for the "general" examination of the bankrupt before adjudication. Under the Amendment of 1910, even before the decision of the Supreme Court in *Cameron v. United States*, it was manifest that, in instances of compositions in bankruptcy without adjudication under Bankruptcy Act, § 12 (a), the bankrupt could have been put under general examination before adjudication.

§ 1544. No Notice Requisite Where Bankrupt Witness upon Issues between Parties.—No notice to creditors is necessary where the bankrupt is called to testify as a mere witness upon some issue between parties in the case.

The statutory requirement that ten days' notice by mail must be given to creditors "of all examinations" of the bankrupt, is probably to protect the bankrupt from vexatious repetitions of examination by different creditors,³⁶ and does not refer to cases where the bankrupt may be needed as a witness to testify for or against some particular issue between parties in the proceedings, but refers to what is termed the "general examination" of the bankrupt, where the bankrupt is put upon the stand and asked miscellaneous questions in a general inquiry concerning his affairs, where no issue is raised, where nothing is to be proved and where no judgment or order results. Of course, whenever a party needs the bankrupt's testimony to support or defend some claim or right, the party is entitled to the testimony of the bankrupt, precisely as much as to that of any other necessary witness; and no notice to creditors is required—a simple subpoena at most is all that is needed to bring the bankrupt.

§ 1545. Bankrupt Examined without Notice before First Meeting, in Relation to Pending Application.—In this way a bankrupt may

him to be a bankrupt because, if upon a trial of the fact of bankruptcy, he should be decided not a bankrupt, of course all the proceedings would become irregular.

"An examination under the order as made in this case, is something which necessarily grows out of the administration of the law, which gives to the Court under certain circumstances prescribed therein, power over the person and property of the debtor, for the purpose of protecting the rights of creditors. * * * Independently of the 26th section, however, it would seem to follow as a necessary consequence, from the general scope of the bankrupt law, that circumstances might exist after the commencement of proceedings in bankruptcy, and after the debtor is brought within the control of the Court, which would warrant an immediate examination. * * *

"The bankrupt law allows proceed-

ings in bankruptcy to be commenced under a certain state of facts. * * * That being done, a prima facie case exists, and then the law clothes the Court with all the powers necessary to accomplish the great object in view, namely, to protect the general creditors of the debtor by discovering and taking possession of all his property for equal distribution among them.

"One of the principal objects of the law would be frustrated if adequate means were not provided for the ascertainment of all the facts affecting the property of the debtor. * * *

"So that, on the whole, in view of the purpose of the 26th section, and the general scope of the bankrupt law, I can not doubt the existence of the power exercised, in the instance, by the District Court."

³⁶ In re Price, 1 A. B. R. 419, 91 Fed. 326 (D. C. N. Y.).

be examined as a witness before he has filed his list of creditors, in aid of some application or motion of some party to the proceedings. Thus, it has been held allowable to examine him, without notice to creditors, for the purpose of gathering the information requisite to fill out the bankrupt's own schedules;³⁷ and to direct the bankrupt to furnish information to aid the court and its officer, the receiver, in the preservation of the estate for creditors, without the giving of notice.³⁸

§ 1546. **Also, Even before Adjudication.**—And even before adjudication.³⁹

§ 1547. **Broad Scope of General Examination**—"Acts, Conduct and Property."—No rigid rules can be laid down as to the method and scope of the general examination of the bankrupt and witnesses.⁴⁰

In *re Foerst*, 1 A. B. R. 259, 93 Fed. 190 (D. C. N. Y.): "There is no precise rule governing the admissibility of such testimony, other than that it should be reasonably pertinent to the subject of inquiry. In general, a large latitude of inquiry should be allowed in the examination of persons closely connected with the bankrupt in business dealings, or otherwise, for the purpose of discovering assets and unearthing frauds, upon any reasonable surmise that they have assets of the debtor. The intent of the Bankrupt Law is that only the honest debtor shall be discharged; and that any proper assets of the estate, however concealed, shall be made available to creditors. The examination for this purpose is of necessity, to a considerable extent, a fishing examination. The extent to which it shall be permitted to go must be determined by the sound judgment of the officer before whom it is taken. Reasonable examination should not be allowed to be checked by constant objections that the materiality of the answer may not be immediately apparent, where no harm can arise to the witness from the disclosure, if the transaction is honest. If the result of such an examination may often be a considerable amount of immaterial testimony, this is a much less evil than to stifle examination by technical rules which would defeat the purpose of the act, and discredit the administration of the law in the interest of creditors. Unreasonable discursiveness in the examination will be in some measure checked by making it at the expense of the examining party; if plainly frivolous, or prolix, it should be stopped. Where questionable proceedings have been disclosed, greater latitude in the prosecution of inquiries should be allowed; and the precise form or order in which the questions are put can scarcely be deemed material.

"Upon the above general principles, and upon the matters already disclosed on this examination, I think the witness should answer as respects any moneys or property acquired by her during the year prior to the adjudication, or even farther back, should further testimony show such inquiries to be reasonably pertinent."

Compare, In *re Williams*, 10 A. B. R. 538, 123 Fed. 321 (D. C. Tenn.): "It is proper to remark here that the ordinary provisions of law for taking the testimony of absent witnesses contemplate their examination as witnesses to

37. In *re Franklin Syndicate*, 4 A. B. R. 244, 101 Fed. 402 (D. C. N. Y.).

38. *Abrahamson v. Bretstein*, 1 A. B. R. 44 (Ref. N. Y.); In *re Fixen & Co.*,

2 A. B. R. 822, 96 Fed. 748 (D. C. Calif.).

39. In *re Fixen & Co.*, 2 A. B. R. 822, 96 Fed. 748 (D. C. Calif.).

40. Bankr. Act, § 21 (a).

prove definite issues made by the pleadings in the case in which they are examined as witnesses. But in bankruptcy proceedings, while the scope of their examination is much broader, the purpose is none the less definite, although peculiar to bankruptcy proceedings. While they are witnesses in every sense of the word, they are examined inquisitorially for the purpose of discovering what general or specific knowledge they have of the bankrupt's affairs and property; or, to use the language of § 21 of the Act of 1898, they are examined at large 'concerning the acts, conduct, or property of a bankrupt.' There may be no action at law or bill in equity or libel in admiralty or other like proceedings in which they are examined as witnesses upon issues made by pleadings in the ordinary way but there is pending, in the bankruptcy court upon pleadings appropriate to that purpose, the administration of a bankrupt estate about which the trustee needs information from those who have knowledge of the bankrupt's affairs, and every bankruptcy system provides for an inquisitorial examination of all those wherever present who had such knowledge. It is this kind of examination which is provided for by the bankruptcy statute and procured by the ordinary practice for the taking of the testimony of witnesses when they reside beyond the jurisdiction of the court."

No issue is involved. No fact is asserted on one side and denied on the other. No fact is to be proved or disproved. The examination is simply a general inquiry into the "acts, conduct and property of the bankrupt," the cause of his failure, the whereabouts of his property, the contracts relating to his business, and in short an examination into all matters and things of reasonable interest to the creditors;⁴¹ and, as a consequence, a great latitude of inquiry is permitted.

U. S. v. Wechsler, 16 A. B. R. 5, — Fed. — (D. C. N. Y.): "In the case of a trial upon issues framed it must be material to those issues, but this section of the Bankrupt Act, you will perceive, does not provide for any trial. There is no decision to be made necessarily as the result of the giving of this evidence. It is an investigation. He is to be examined concerning the acts, conduct or property of the bankrupt. It is a broad field of inquiry and intended to be so, and this section is the section under which the investigations usually take place about the property of the bankrupt, particularly in cases where there is any suspicion that there has been any attempt to take property and conceal it from creditors. * * * If there have been recent transfers of property or payments of money on the eve of bankruptcy, that is a suspicious fact, particularly if they have been transferred to relatives or connections. All such transfers become material subjects of inquiry; and in order to ascertain what the truth is about them the party examining the bankrupt is not confined to a mere inquiry in the first instance whether the property has been transferred, or a mere explanation of what it was transferred for, but counsel have a right to inquire into all the surrounding circumstances in the case in order to ascertain what the truth is in that respect."

In re Horgan & Slattery, 3 A. B. R. 253, 98 Fed. 414 (C. C. A. N. Y.): "The provisions of the Bankruptcy Act authorizing the examination of third persons as witnesses, and compelling the production of books and documents upon such examinations, are intended to enable creditors to discover transactions which may effect the right of the bankrupt to obtain a discharge, and to enable

41. Inferentially, In re Rose, 19 A. B. R. 169 (D. C. Pa.).

the trustee to ascertain whether any assets exist which should be collected and applied toward the payment of the bankrupt's debts. It is the duty of the Bankruptcy Court to see that such examinations are not permitted to transcend the limit of a legitimate investigation for these purposes; but of necessity this is a duty which involves the exercise of a wide discretion, and which should not be interfered with by an appellate court except when it has been manifestly abused."

Obiter, In re Carley, 5 A. B. R. 554, 106 Fed. 862 (D. C. Ky.): "Speaking generally, I think the provisions of § 21a of the Bankruptcy Act should be liberally construed, so as to enforce full and frank answers by witnesses who are being examined under its provisions as to the 'acts, conduct or property of the bankrupt,' the object being to secure information on those subjects for use in the administration of the bankrupt's estate. The statute was intended for beneficial purposes, and in order to affect them witnesses should fully disclose all their knowledge relative either to the acts, the conduct or the property of the bankrupt."

Obiter, In re Wilcox, 6 A. B. R. 362, 366, 109 Fed. 628 (C. C. A. N. Y.): "The right of the trustee extends to a discovery of whatever tends to bring to light the estate of the bankrupt so as to enable the trustee to pursue the estate and reduce it to possession and to enable creditors 'to discover transactions which may affect the right of the bankrupt to obtain a discharge.'"

Compare, *obiter*, In re Rauchenplat, 9 A. B. R. 763 (D. C. Porto Rico): "Great latitude should be allowed in evidence to find a bankrupt's assets, or unearth fraud, but the court, or if acting by its referee, has a discretion how far this should proceed, and the referee had a legal discretion as to the extent of the examination of the books of the witness."

The examiner is not bound to state what he expects to prove by any of his questions. He is not trying to prove anything. He is simply inquiring and informing himself about his debtor's affairs.⁴²

In re Fixen & Co., 2 A. B. R. 832, 96 Fed. 748 (D. C. Calif.): "The examinations thus provided for are not intended as means of producing testimony pertinent to issues then on trial, but their object is to afford to the creditors, and the officer charged with administering the trust, full information touching the bankrupt's estate in order that necessary steps may be taken for its possession and preservation."

Impliedly, In re Jacobs & Roth, 18 A. B. R. 728, 154 Fed. 988 (D. C. Pa.): "In the course of the examination of Jacob Jacobs, one of the bankrupts, Mr. Sachs, representing certain of the creditors, showed the witness a paper, being a statement of credit made to the Fushan-Zeman Shoe Company in September last, and asked him if he had signed it. Objection was made to the question and the referee ruled that the witness was entitled to at least a statement of the purpose, to which Mr. Sachs replied, 'Purpose to show that the witness made a written statement on or about September 4th, 1906, that it is material, that the testimony given by him at this hearing as regards the financial condition of the partnership about said time,' presumably meaning thereby that it is material with reference to the testimony given by him at this hearing to know the financial condition of the partnership about said time. The referee ruled

⁴². [1867]. In re Earl, Fed. Cases, No. 4244; [1867] In re Krueger, Fed. Cases, No. 7,942; [1867] In re Lathrop, Fed. Cases, No. 8,106; [1867] In re Stuyvesant, Fed. Cases, No. 13,582;

[1867] In re Mendenhall, Fed. Cases, No. 9423; In re Bryant, 26 A. B. R. 504, 188 Fed. 530 (D. C. Pa.), quoted at §§ 1526, 1540, and particularly at § 1541.

that this question had relation more to an application for discharge than to an examination of the bankrupt at this time, and sustained the objection. The offer was then renewed and the further reason given that it is for the purpose of proving that on the strength of the written statement offered the bankrupt obtained credit and merchandise from one of the present creditors and that this is within the scope of the purpose of an examination of the bankrupt, which is for the purpose of disclosing all his affairs and dealings with his creditors. Upon the objection being renewed, it was again sustained, and a certificate asked for. The very clause of the Bankrupt Act quoted by the referee authorizes the examination of the bankrupt as to any matter which will aid his creditors in ascertaining what has become of the property with which at any time within a reasonable period prior to the bankruptcy proceedings he has certified himself as being possessed of, in order to enable them to ascertain whether or not he has been guilty of making fraudulent disposition of his property or otherwise disposing of the same to their prejudice and also to learn generally regarding the character and amount of his estate at that time as compared with the present and his conduct and disposition thereof in the meantime."

The only limitation upon the inquiry is that it shall be pertinent to the acts, conduct or property of the bankrupt in some way.

In *re Howard*, 2 A. B. R. 582, 585, 95 Fed. 415 (D. C. Calif.): "Of course, when the person whose attendance is required appears before the referee, his examination must be relevant to matters concerning the acts, conduct, or property of the bankrupt, and it must be presumed that the referee will confine the examination within legal limits; that is, within limits pertinent to such general inquiry, and the witness will be justified in refusing to answer irrelevant or impertinent questions."

Of course, questions relating to his religion or to his domestic infelicities or to his politics are improper. Also questions whose answers could not in any way throw light on any present assets or on any act that would prevent discharge;⁴³ so, also, would it be improper repeatedly to cover the same ground.⁴⁴

The examination should be decorous and decent, and should not be unduly prolonged nor unnecessarily vexatious. This is about all that can be said as to the nature of the general examination of the bankrupt and witnesses.

In *re Jacobs & Roth*, 18 A. B. R. 728, 154 Fed. 988 (D. C. Pa.): "It is not intended by this to state that a general voyage of discovery is to be authorized covering any and every period of the bankrupt's business dealings and transactions, but only such as within a reasonable time of the bankruptcy proceeding can fairly be taken to shed some light upon his affairs at that time."

Of course, as before stated, when the bankrupt is called as a witness in support of some issue raised between parties to the proceedings, then the rules for his examination are the same as for any other witness and the fact that it is the bankrupt who is testifying will not alter the rules except, perhaps, in so far as he may or may not be considered an interested party.

The subject of the examination is to be confined to the acts, conduct and

⁴³. In *re Hayden*, 1 A. B. R. 670, 96 Fed. 199 (D. C. N. Y.).

⁴⁴. In *re Romine*, 14 A. B. R. 789, 138 Fed. 837 (D. C. W. Va.).

property of the bankrupt and his dealings with his creditors, etc., preceding the adjudication; nevertheless, facts occurring subsequently thereto also may be inquired into if in their nature they are such as would likely throw light on the acts, conduct or property of the bankrupt *before* the adjudication, or on the amount, kind and whereabouts of the property.⁴⁵

The examination is not limited to transactions occurring within the four months preceding the bankruptcy. A full understanding of the acts, conduct and property of the bankrupt may involve inquiry into facts occurring months and even years beforehand.⁴⁶

And it must not be forgotten that he may be examined, too, as to "all matters that may affect the administration and settlement of his estate."^{46a}

§ 1548. Production of Books, Papers and Documents Enforced.—The production of books, papers and documents may be enforced. As to the bankrupt's books, documents, etc., the Act itself vests their title in the trustee.⁴⁷

Third parties, examined as witnesses, may be required to produce their books of account, where showing has been made that property probably has been turned over to them in violation of the Bankruptcy Act. Perhaps mere circumstances of suspicion may suffice to lay a predicate for the production.

And even such showing is not, on principle, necessary if the books also involve transactions with the bankrupt, or in which the trustee is interested. Thus, the minute book of a corporation has been ordered produced.

In *re United States Graphite Co.*, 20 A. B. R. 280, 159 Fed. 300, 161 Fed. 583 (D. C. Pa.): "The referee is engaged in making inquiry as to an alleged fraud between the Pennsylvania Graphite Company, whose minute book is required, and the bankrupt estate, and further, the corporation—the owner of the minute book—is also interested in having an order made for security for payment of rent. So that in these two questions under investigation, if not in the others, the Pennsylvania Graphite Company is a party to this litigation, and is required, in response to the subpœna for that purpose, to produce such specified books and papers as bear upon the questions investigated. When the book has been produced before the referee, of course, counsel, intending to establish certain facts from this minute book, is entitled to see it and to examine its contents for the purpose of ascertaining what it contains in relation to the questions at issue.

45. Impliedly, *In re Walton*, 1 N. B. N. 533. Compare, under law of 1867, *In re McCrien*, Fed. Cas. 8,666, 3 N. B. Reg. 90; (1867) *In re Rosenfield*, 1 N. B. Reg. 60, Fed. Cas. 12,059.

46. *In re Brundage*, 4 A. B. R. 47, 100 Fed. 613 (D. C. Iowa); *In re Pursell*, 8 A. B. R. 96, 114 Fed. 371 (D. C. Conn.).

46a. Bankr. Act, § 7 (9).

47. Bankr. Act, § 70 (a) (1). See ante, § 956. *In re Fixen & Co.*, 2 A.

B. R. 822, 96 Fed. 748 (D. C. Calif.); compare, *In re Romine*, 14 A. B. R. 792, 138 Fed. 837 (D. C. W. Va.).

See instance of contempt for failure to produce, the bankrupt's excuses not being accepted as reasonable by the court, *In re Alper*, 19 A. B. R. 612, 162 Fed. 207 (D. C. N. Y.).

Instance, *In re Hyman J. Herr* (No. 1); 25 A. B. R. 141, 182 Fed. 715 (D. C. Pa.); *In re Soloway & Katz*, 28 A. B. R. 229, 196 Fed. 132 (D. C. Conn.).

An indiscriminate call for a book or paper which, upon its face, could in all probability have no bearing upon the questions investigated, would be improper, and an objection to its examination by counsel for an adverse party would be sustained, but where it appears that the books or paper called for is so obviously the document containing the truthful information concerning the questions investigated, it is clearly the right of counsel to examine the book or paper to see what it discloses as to the matters at issue."

It has been held, though it is a somewhat dangerous precedent, that an officer of a corporation of which the bankrupt was a stockholder can not be compelled on "general examination" of the bankrupt to produce the corporation's books, etc., for the purpose of enabling the trustee to ascertain the value of the stock.⁴⁸ However, were a controversy pending wherein the value of the stock should become of importance, undoubtedly such enquiries might become proper on general examination as an aid to the trustee, for it is the function of a general examination to aid the trustee in realizing on the assets.

And claimants proving debts to share in dividends must produce their books and documents that are pertinent to the claims.⁴⁹

In *re Wheeler*, 19 A. B. R. 461, 158 Fed. 603 (C. C. A. Conn.): "The president of the bank was on the stand and the book was within his control, being in the hands of his counsel. Said counsel testified that the book did not belong to the bank, but was the president's personal property, containing a mere compilation from the books of the bank, a mere mathematical computation or calculation. Manifestly this statement is largely hearsay; whether the book contains original entries or merely compilations from other entries could be told only by one who knew when and under what circumstances the entries were made. The president himself testified that the book was one which 'he kept during all the time that these payments were being made,' that the 'payments were entered therein as they were made,' and that the entries were in the handwriting of the president or the cashier. Under these circumstances the evidence was competent, certainly as to details of date and amount which could not be carried by the unaided memory; and it should have been produced. Whether or not any particular entry was obnoxious to some valid objection, was a question to be determined by the referee with the book before him."

§ 1549. Whether Federal Equity Rules Govern "General" Examinations.—General Order No. XXII provides that the "examination and cross-examination of the witnesses shall be had in conformity with the mode now adopted in courts of law of the United States," that mode being prescribed by U. S. Rev. Stat., § 721, as follows:

"The laws of the several States, except where the Constitution, treaties or statutes of the United States otherwise require or provide, shall be regarded as rules of decision in trials at common law, in the courts of the United States, in cases where they apply."

Yet it is doubtful whether this rule adopts the common-law federal rules,

⁴⁸. In *re Seligman*, 26 A. B. R. 664, 192 Fed. 750 (D. C. N. Y.).

⁴⁹. In *re Clark*, 21 A. B. R. 776 (Ref. Calif.).

in toto, whereby the mode of examination and cross-examination of witnesses prevailing in the courts of the particular State is accepted in the federal court.⁵⁰

And, in the so-called "general examinations" of the bankrupt and of witnesses, it is doubtful whether the strict rules of *Dravo v. Fabel*, 132 U. S. 489, as to taking the opposite party's deposition, apply. The relevancy or irrelevancy of questions is for the court to determine.⁵¹

§ 1550. Witness Not Excused because Testimony Would Reveal Private Affairs.—A witness will not be excused from answering an apparently relevant question because of his assertion that the answer would disclose the personal affairs of himself or others, not material to the subject of inquiry;⁵² nor from producing books or documents, for the same reason.⁵³

§ 1551. But Examiner Must Develop Facts Showing Sufficient Connection with Bankrupt to Make Further Inquiry Relevant.—But, after the witness has positively negated the idea that the matter inquired into has any relation to the acts, etc., of the bankrupt, it devolves upon the examiner to develop facts showing sufficient connection with the acts, conduct or property of the bankrupt to make further inquiry reasonably relevant.⁵⁴

In *re Carley*, 5 A. B. R. 556, 106 Fed. 862 (D. C. Ky.): "But the act does not demand such liberality of construction when it is sought to inquire into the acts, conduct or property of any persons other than the bankrupt himself. Indeed, the act does not authorize, in this mode of proceeding, any examination whatever into matters other than those specifically mentioned, which might, however, include cases where the acts, conduct or property of the witness are so connected or interwoven with those of the bankrupt as to make them virtually the same by reason of community of interest."

Compare, as to practice on opposition to discharge, *In re Romine*, 14 A. B. R. 785, 138 Fed. 837 (D. C. W. Va.): "It has been settled beyond peradventure for very many years that courts do not compel production of books simply to gratify curiosity, or permit 'fishing' excursions into them to see what can be found that may or may not be of advantage to the parties making the demand. A party cannot obtain a roving commission for the inspection or production of books or papers in order that he may ransack them for evidence to make out his case. He is entitled to production and inspection only when the same is material and necessary to establish his cause of action. The application will not be granted where the facts to be proved by the books can be otherwise established. It will therefore be denied when the party has in his possession or under

50. Compare, inferentially, *In re De-Gottardi*, 7 A. B. R. 739, 740, 114 Fed. 328 (D. C. Calif.).

51. *People's Bank v. Brown*, 7 A. B. R. 475, 112 Fed. 652 (C. C. A. N. J.).

52. *People's Bank v. Brown*, 7 A. B. R. 475, 112 Fed. 652 (C. C. A. N. J.). Compare, *In re Howard*, 2 A. B. R. 582, 585, 95 Fed. 415 (D. C. Calif.).

53. *In re Fixen & Co.*, 2 A. B. R. 822, 96 Fed. 748 (D. C. Calif.).

54. Compare, *In re Fixen & Co.*, 2 A. B. R. 822, 96 Fed. 748 (D. C. Calif.). Apparently rule taken for granted, *In re United States Graphite Co.*, 20 A. B. R. 280, 159 Fed. 300, 161 Fed. 533 (D. C. Pa.), quoted at § 1548.

his control the means of acquiring all the information he seeks to obtain, or when the books do not in themselves contain evidence, but merely information by which evidence can be obtained. It is not permitted to enable a party to ascertain whether he has cause of action or defense, or to ascertain the evidence on which his opponent's action or defense rests."

But proof in advance of the existence of any particular interest or right or relation between the witness and the bankrupt estate is not requisite so long as the circumstances developed might, with other circumstances to which the inquiries are directed, lay a foundation if true, for recovery of assets or for proof of such acts as might bar discharge or affect the claims of parties.

Inferentially, *People's Bk. v. Brown*, 7 A. B. R. 476, 112 Fed. 652 (C. C. A. N. J.): "It is true that when the appellee was interrogated respecting this real estate it had not been shown that the bankrupt had any interest in it; but his relationship to the parties, to several transactions concerning it, the history of those transactions, and the communications which ensued between the bankrupt and the witness when the latter was served with a subpoena, did appear, and disclosed a state of facts which justified the investigation. Its object was to determine whether the bankrupt did not have an interest in the property which should be applied to the payment of his debts, and the discovery sought would have been superfluous if, as a condition precedent to its requirement, it had been necessary to independently establish the existence of such interest. Although it is the duty of the court to confine such examinations within the limits to which the purposes for which they are authorized restrict them, yet, where there are circumstances warranting the investigation, no obstruction of it should be permitted which is not justified by law. * * *

"The relevancy of any particular matter to the subject under judicial investigation is always for determination by the court, and no witness is entitled to decide for himself that the facts which he is asked to disclose would tend to prove the existence or nonexistence of the ultimate fact to which it is intended to relate them. * * * 'It is, in substance, but an expression of his understanding that the facts which he declines to reveal would, if revealed, appear to be immaterial, and to this opinion of his, though not even evidential, he asks that there shall be conceded determinative force.'"

§ 1552. Whether General Examinations to Be in Writing.—It would seem that, as a rule, the general examinations of witnesses and bankrupts are to be taken down in writing, by or under the direction of the referee, in the form of a deposition, and that they may be in narrative form;⁵⁵ or by question and answer. But it has been held, on the other hand, to be a matter resting in the sound discretion of the referee, whether the examination shall be oral or be taken in writing.⁵⁶ And such would seem to be the reasonable rule.

Undoubtedly, the requirement that it be taken in writing may be waived by counsel of both parties.⁵⁷ Other examinations, taken upon issues joined,

55. Gen. Ord. XXII; In re Romine, 14 A. B. R. 785, 138 Fed. 837 (D. C. W. Va.).

56. In re Goldstein, 19 A. B. R. 96, 155 Fed. 695 (D. C. N. Y.).

57. Compare, inferentially, obiter, In re Wilcox, 6 A. B. R. 366, 109 Fed. 628 (C. C. A. N. Y.).

are not subject to this requirement.

The deposition must be read over to the bankrupt or other witness, and signed by him in the referee's presence.⁵⁸

The bankrupt or other witness should always be permitted to make a correction in any statement theretofore made and the reason therefor may be taken into consideration by the court in passing upon the credibility of the witness.⁵⁹ Such correction, however, does not permit the bankrupt or other witness to expunge the corrected parts, if they accurately state the testimony actually given, but simply permits the addition of the statement that the former testimony was incorrect and should have been given differently, "as now stated."

§ 1553. Objections to Be Entered on Record.—Objections made must be entered on the record by the referee, together with his rulings thereon.⁶⁰

The ground of objection must, in general, be stated, else exception will not be available on review.⁶¹ Where, however, there is only one possible ground and that one is sufficiently obvious, the reviewing court may consider the objection.⁶²

§ 1554. Referee to Rule on Admissibility and to Exclude Incompetent Testimony.—But the referee is to pass upon the admissibility of evidence offered and to exclude that which is incompetent, irrelevant or otherwise inadmissible.⁶³

In *re Wilde's Sons*, 11 A. B. R. 714, 131 Fed. 142 (D. C. N. Y.): "This motion involves the question whether a referee in bankruptcy has any power to exclude evidence. As I understand it, an officer appointed to simply take testimony for the use of the court, as, for instance, an examiner in an equity suit, has no jurisdiction to exclude or pass upon testimony. Unless the parties refer any question of the admission of testimony to the court, he is obliged to take all that is offered. But I think that whenever any officer is appointed whose duty it is to take evidence and also to exercise any judicial duty in regard to it, as to decide issues or to state the facts or law in an opinion or report, it is his right and duty to exclude inadmissible evidence upon objection. Why should he admit evidence which it would be his duty to disregard if admitted? Substantially all the cases in which evidence is taken by referees in bankruptcy, either in their character as referees or as special commissioners, are cases in which they either decide questions outright or draw conclusions from the evidence in the shape either of a report or an opinion; and I

58. Gen. Ord. XXII.

59. In *re Hark Bros.*, 14 A. B. R. 625 (D. C. Penn.).

60. Gen. Ord. No. XXII.

61. Equity Rule XI of Circuit Court of Appeals, 150 Fed. XXVII; see also, inferentially, In *re Clark*, 21 A. B. R. 776 (Ref. Calif.).

62. *Johnson v. United States*, 20 A. B. R. 724, 163 Fed. 30 (C. C. A. Mass.).

63. See ante, § 552. Compare, In *re DeGottardi*, 7 A. B. R. 742, 114 Fed. 328 (D. C. Calif.); apparently contra, In *re Romine*, 14 A. B. R. 785, 138 Fed. 837 (D. C. W. Va.). But this case does not seem to note the distinction between the referee acting in his ordinary functions and as special master on discharge. Compare, however, *National Bank v. Abbott*, 21 A. B. R. 436, 165 Fed. 852 (C. C. A. Mo.).

think that in all such cases the referee has the right to exclude evidence which he deems inadmissible. If error is committed by such exclusion, any party interested can take up the matter immediately on a certificate, or can urge the alleged error on final hearing. I am aware that there are authorities to the contrary for which I feel sincere respect, but none of them is necessarily controlling upon me, and I am not able to concur with them. The delay and expense of a bankruptcy system under which a referee has no power to exclude testimony, however irrelevant, is so great that such a method of procedure should not be permitted unless the principles of law absolutely require it. In my opinion they do not require it in proceedings before referees in bankruptcy."

In *re Ruos*, 20 A. B. R. 281, 159 Fed. 252 (D. C. Pa.): "A word upon the practice before referees may be appropriate. Where a question arises concerning the competency of a witness, or the admissibility of evidence, the referee should decide the point himself in the first instance instead of turning the matter over to the court. It will be time enough to certify the question when he is asked to do so in a proper manner. Very often his ruling will be acquiesced in, and the delay of referring the dispute to the court will thus be avoided."

But compare, *Missouri, Am. Elec. Co. v. Hamilton Brown Co.*, 21 A. B. R. 270, 165 Fed. 283 (C. C. A. Mo.): "It is the duty of examiners, masters, referees, and the court taking evidence in controversies in bankruptcy, in the absence of a jury, to take, record, and, in case of an appeal, to return to the reviewing court, all the evidence offered by either party, that which they hold to be incompetent or immaterial as well as that which they deem competent and relevant, to the end that if the appellate court is of the opinion that evidence rejected should have been received it may consider it, render a final decree, and thus conclude the litigation without remanding the suit to procure the rejected evidence. From this rule evidence plainly privileged, the testimony of a privileged witness, and evidence which clearly and affirmatively appears to be so incompetent, irrelevant, or immaterial that it would be an abuse of the process or power of the court to compel its production or permit its introduction, are excepted."

Apparently, *contra*, In *re Sturgeon*, 14 A. B. R. 682, 139 Fed. 608 (C. C. A. N. Y.): "Under General Order No. 22 (18 Sup. Ct. vii), the duty of the referee is to receive the evidence which is offered, to note objections and to record the evidence; and, if either party persists in offering incompetent or irrelevant matter in evidence, the other party has a remedy, because the rule provides that 'the court shall have power to deal with the costs of incompetent, immaterial or irrelevant depositions, or parts of them, as may be just.' The equity practice is to be followed by referees. The order directs him to proceed as referee. The referee must take all the evidence and note objections." But it is to be noted that this was an examination before a referee in another district than the one wherein the bankruptcy was pending and this might afford a distinction.

At any rate, the referee is to exclude evidence that is so clearly incompetent, irrelevant or immaterial that it would have been an abuse of the process or power of the court to have compelled its production.⁶⁴

A rule compelling the referee on general examinations of bankrupts and witnesses, to take down answers, although the questions be incompetent and the answers improper, would lead to interminable confusion, and would practically give over such examinations into the absolute control of the

64. In *re Clark*, 21 A. B. R. 776 (Ref. Calif.).

examiner, leading to the possibility of intolerable abuse. The distinction noted in *In re Wilde's Sons*, *supra*, undoubtedly states the true principle.⁶⁵

§ 1555. General Examination Competent as Admission in Subsequent Litigation against Same Party.—The written deposition taken on general examination and also verbal testimony as to what was testified to on general examination, either of the bankrupt or of any witness, is admissible in evidence, as an admission, in any proceeding against the particular party so previously testifying.⁶⁶

In re Alphin & Lake Cotton Co., 12 A. B. R. 653, 131 Fed. 824 (D. C. Ark., affirmed in 14 A. B. R.): "Their testimony taken under § 7 or § 21—they having the right under the Act to have the assistance of counsel, at the expense of the estate, if necessary, and an opportunity for cross-examination—was clearly admissible in any proceeding against them, other than criminal, as admissions against themselves."

In re Wilcox, 6 A. B. R. 366, 109 Fed. 628 (C. C. A. N. Y.): "The testimony of the bankrupt himself, which is ordinarily reduced to writing by or under the supervision of the referee, and given under the solemnity of an oath, amounts, when protection against criminative testimony has been waived, to his admission, which can be used elsewhere, but not in any criminal or penal proceeding, as in admission against himself (*In re Krueger*, 2 Lowell 182)."

But is not admissible as against any other party.⁶⁷

65. But compare the practice on hearings in opposition to discharge before referees acting as special masters and where depositions are being taken in one district for use in a bankruptcy proceedings pending in another district, where the rule seems to be that if objection is made and sustained and exception taken the special master is bound nevertheless to take down the answer offered noting the objection thereto, the exception and his rulings.

In re Romine, 14 A. B. R. 785, 138 Fed. 837 (D. C. W. Va.): "It is clear to me that in taking testimony the referee must have it taken down, preferably in narrative form, but, upon objection raised, it is his duty to require the matter to be presented by question, to which the objection and reason thereof is to be clearly but briefly noted; then to enter his ruling thereon as to whether proper or not, and, although he may rule it to be improper, yet allow it to be answered. I am persuaded, however, that he is not called upon to suffer and allow counsel, as in this case, to ask and permit witnesses to answer the same question over and over again, whereby time is unnecessarily consumed and costs incurred; but that upon his notice the fact that the question has been once answered, of the demand to answer has been once

positively refused, the court will justify him in preventing vain repetition."

In re Lipset, 9 A. B. R. 32, 119 Fed. 379 (Ref. N. Y., affirmed by D. J.); *In re DeGottardi*, 7 A. B. R. 723, 114 Fed. 328 (D. C. Calif.); *In re Sturgeon*, 14 A. B. R. 681, 139 Fed. 608 (C. C. A. N. Y.). But compare, *post*, § 1571.

66. See *post*, §§ 1747, 1839. See also, *infra*, § 1839. *In re Wiesen Bros.*, 14 A. B. R. 347, 135 Fed. 442 (D. C. Penn.); *In re Gaylord*, 7 A. B. R. 1, 112 Fed. 668 (C. C. A. N. Y., affirming 5 A. B. R. 410); *In re Mellen*, 3 A. B. R. 226, 97 Fed. 326 (D. C. N. Y.); *In re Dow*, 5 A. B. R. 400, 105 Fed. 889 (D. C. Iowa). See *post*, § 1839. *Contra*, but because considered to be privileged, *In re Marx*, 4 A. B. R. 521, 102 Fed. 676 (D. C. Ky.). *Contra*, but because considered to be privileged, *In re Logan*, 4 A. B. R. 525, 102 Fed. 876 (D. C. Ky.).

67. See *post*, § 1747; also see *In re Wilcox*, 6 A. B. R. 362, 109 Fed. 628 (C. C. A. N. Y.); *In re Alphin & Lake Cotton Co.*, 12 A. B. R. 653, 131 Fed. 824 (D. C. Ark., affirmed in 14 A. B. R.); *In re Wiesen*, 14 A. B. R. 347, 135 Fed. 442 (D. C. Penn.); *Taylor, trustee v. Nichols*, 23 A. B. R. 310, 134 App. Div. (N. Y.) 787. *Contra*, *In re Cooke*, 5 A. B. R. 434, 109 Fed. 631 (D. C. N. Y., following *In re Wilcox* before rehearing of latter case

Breckons v. Snyder, 15 A. B. R. 112, 211 Pa. St. 176: "The notes of the testimony of the bankrupt, taken at a preliminary proceeding before the referee, to ascertain his assets and liabilities, were properly rejected. The issue was not between the same parties, nor did it involve the same subject matter."

In *re Hersey*, 22 A. B. R. 863, 171 Fed. 1001 (D. C. Iowa): "Upon the hearing of the claim, and the objections of the trustee thereto, the testimony of the bankrupt and other witnesses examined before the referee at the first and other meetings of the creditors was offered by the trustee and admitted in evidence over the objections of the petitioner that no notice had been given him that such testimony was to be used in any proceeding whatever against him. Hart [the claimant] was also examined at such meeting, and was present at the examination as attorney for the bankrupt while the latter was being examined, but was not present when the others were examined, and was not notified at any time before the testimony was taken that it was to be used against him. It seems clear that, aside from his own examination, none of this testimony was admissible against the petitioner upon the hearing of this claim, and it will not be considered as against him."

And is admissible even though not in writing nor signed if proved by the testimony of those who heard it.⁶⁸

§ 1555½. But Not to Be Considered unless Actually Introduced or Stipulated in.—But the general examination is not to be considered as in evidence, though taken before the same referee in the same bankruptcy, unless actually introduced in evidence or stipulated in, in the particular controversy then under consideration.⁶⁹

§ 1556. Bankrupt's Testimony Not to Be Used in Criminal Proceedings against Him.—No testimony given by the bankrupt shall be offered in evidence against him in any criminal proceedings.⁷⁰

The Supreme Court of the United States has interpreted this clause as

—distinguished in *In re Wiesen*, 14 A. B. R. 347, 135 Fed. 442, D. C. Penn.).

Instance, *contra*, but point not specifically passed upon. *Collett v. Bronx Nat. Bk.*, 29 A. B. R. 454, 200 Fed. 111 (D. C. N. Y.).

Contra, and that the evidence on general examination given by a bankrupt, since deceased, may be introduced against the trustee on reclamation proceedings, see *In re Thompson*, 28 A. B. R. 794, 197 Fed. 681 (D. C. N. J.).

68. *Obiter*, in *re Bard*, 5 A. B. R. 810, 108 Fed. 208 (D. C. N. Y.); *obiter*, in *re Knaszak*, 18 A. B. R. 189, 151 Fed. 503 (D. C. N. Y.).

69. In *re Murray*, 20 A. B. R. 700, 162 Fed. 983 (D. C. Conn.); In *re Wolder*, 18 A. B. R. 419, 152 Fed. 489 (D. C. Conn.); see *ante*, § 553.

70. Compare, *post*, § 2324.
Bankr. Act, § 7 (9): "No testimony given by the bankrupt shall be offered

in evidence against him in any criminal proceedings."

U. S. v. Marsh. Chambers, 13 A. B. R. 708 (D. C. N. Y.): This case extends the doctrine to an unreasonable extent, holding that in a proceeding before a grand jury on an indictment for concealing assets, under § 29, by failing to schedule them, it is unlawful to produce the schedules themselves, as evidence and that an indictment so procured will be dismissed. How can the crime be proved if the very fact itself—*corpus delicti*, so to speak—cannot be given in evidence. It is doubtful if the proviso of § 7 (9) or the constitutional guaranty would extend so far. The immunity from the use of testimony would hardly extend to the use of schedules.

U. S. v. Simon, 17 A. B. R. 41, 146 Fed. 89 (D. C. Wash.). See discussion in *State v. Strait* (Minn.), 102 N. W. 913. Also, in *Burrell v. State*, 12 A. B. R. 132, 194 U. S. 572.

being confined to the "testimony" given upon the examination authorized by the ninth clause of § 7 of the Bankruptcy Act. Under this ruling, therefore, since the repeal of § 860 of the United States Revised Statutes, the schedules of the bankrupt, together with his books and documents, may be used in evidence against him.

Ensign v. Commonwealth of Pennsylvania, 227 U. S. 592, 30 A. B. R. 408: "The reliance of the plaintiffs in error, of course, is upon that part of clause 9 of the section which declares: 'but no testimony given by him shall be offered in evidence against him in any criminal proceeding.'

"It is insisted that, in accordance with the spirit of the Fifth Amendment, this should be construed as applying to the schedule required to be prepared, sworn to, and filed by the bankrupt under the provisions of the 8th clause. But as a matter of mere interpretation, we deem it clear that it is only the testimony given upon the examination of the bankrupt under clause 9 that is prohibited from being offered in evidence against him in criminal proceeding. The schedule referred to in the 8th clause, and the oath of the bankrupt verifying it, are to be 'filed in court' and, therefore, are, of course, to be in writing. The word 'testimony' more properly refers to oral evidence. It was reasonable for Congress to make a distinction between the schedule, which may presumably be prepared at leisure and scrutinized by the bankrupt with care before he verifies it, and the testimony that he is to give when he submits to an examination at a meeting of creditors or at other times pursuant to the order of the court—a proceeding more or less unfriendly and inquisitorial, as well as summary, and in which it may be presumed that even an honest bankrupt might, through confusion or want of caution, be betrayed into making admissions that he would not deliberately make. Full effect can be given to the clause, 'but no testimony given by him shall be offered in evidence against him in any criminal proceeding,' by confining it to the testimony given under clause 9, to which the words in question are immediately subjoined. And, we think that proper interpretation requires their effect to be thus limited."

The immunity cannot be evaded by merely reading questions and answers therefrom and questioning the bankrupt thereon, without introducing the examination itself.

Jacobs v. United States, 20 A. B. R. 550, 161 Fed. 694 (C. C. A. Mass.): "The underlying philosophy of the statute in question is that, as a matter of justice to the bankrupt, and also for the interests of creditors, he should be encouraged to testify freely in his examination; but he would have no encouragement thereto if, on being prosecuted for an offense, he could not undertake to absolve himself by his own testimony except at the risk of being tripped or embarrassed by what he had previously sworn to. To permit a course of cross-examination in the method here, whether the documentary evidence taken before the referee was produced in the presence of the jury or not, would be simply to permit an evasion of the statute, because to do so would involve the mischief which the statute intended to guard against, in that the witness might be more harassed and prejudiced than he would be if the whole document had been frankly put into the case."

Nor is the immunity waived by the bankrupt voluntarily offering himself as a witness.⁷¹

71. *Jacobs v. United States*, 20 A. B. R. 550, 161 Fed. 694 (C. C. A. Mass.).

But this immunity from the use of testimony given by the bankrupt does not prevent prosecution for acts testified to upon examination: the immunity is immunity from the use of evidence so given, not from prosecution.

Burrell v. State, 194 U. S. 572, 12 A. B. R. 132: "It does not say that he shall be exempt from prosecution, but only, in case of prosecution, his testimony cannot be used against him. The two things are different, and cannot be confounded."

In *re Walsh*, 4 A. B. R. 693, 696, 104 Fed. 518 (D. C. S. Dak.): "If the Congress of the United States desires to draw from the bankrupt testimony that may tend to criminate him, it must by legislation provide, under the ruling in the case of *Brown v. Walker*, nothing short of immunity from prosecution. Not that it shall never be used in any criminal proceeding against him, but that he cannot be prosecuted by reason of any information gained in this manner."

But in other cases it has been ably contended that the clause does not grant immunity from prosecution for falseness in the testimony itself thus protected; that the immunity extends simply to its use in a prosecution for any actual crime revealed by the testimony, and is based on such testimony being true.⁷²

Edelstein v. U. S., 17 A. B. R. 658, 149 Fed. 636 (C. C. A. Minn.): "The government contends that the immunity has sole reference to the use of evidence in a prosecution for some offense to which his evidence related; that Congress offered as an inducement to a full, frank, and truthful disclosure by a bankrupt for the benefit of his creditors of all matters and things concerning his property and estate that his evidence should not be used against him in any prosecution for any such offense, however much it might implicate him.

"Defendant's argument is that the language employed is comprehensive and unequivocal; 'that no testimony given by him shall be offered against him in any criminal proceeding;' that it, in terms, prohibits the use of the negative answer given by the bankrupt to the question propounded to him, although knowingly and intentionally false, as a basis for the criminal charge involved in the indictment now under consideration. To this we cannot give our assent. There is no rule requiring a literal construction to be placed even upon unambiguous words of a particular clause of a statute without consideration of its context. The meaning of specific words in one part of a statute is often controlled by other provisions of the same act, and frequently by provisions of other acts which are in *pari materia*. * * *

"Moreover, it would, in effect, secure to the bankrupt the immunity in question for violating his part of the compact, namely, to testify—that is, to testify truthfully—by virtue of which he secured a right to the immunity. We are not willing to impute to Congress any such contradictory and absurd purpose. The words 'any criminal proceeding' cannot sensibly or reasonably be construed so literally and generally as to include the criminal proceeding provided by law for false swearing in giving his testimony."

And the case of *Edelstein v. United States* has been followed.⁷³

⁷² *Wechsler v. United States*, 19 A. B. R. 1, 158 Fed. 579 (C. C. A. N. Y.), reversing *United States v. Wechsler*, 16 A. B. R. 1).

⁷³ *United States v. Brod*, 23 A. B. R. 740, 176 Fed. 165 (D. C. Ga.).

Wechsler v. United States, 19 A. B. R. 1, 158 Fed. 579 (C. C. A.): "The Bankruptcy Act * * *, requires the bankrupt to submit to an examination under oath as to various matters specified therein, with the proviso that 'no testimony given by him shall be offered in evidence against him in any criminal proceeding.' It is contended that the immunity thus accorded in broad, unqualified language should apply to prosecution for falsely testifying upon such examination; and it is suggested that the section quoted from does not contain the qualification found in § 860, Rev. St. U. S. * * * (and in other Federal statutes), that the immunity provision 'shall not exempt any * * * witness from prosecution and punishment for perjury committed in * * * testifying as aforesaid.' Plaintiff in error cites in support of his contention the opinion of Judge Hanford in *U. S. v. Simon* (D. C.), 146 Fed. 89, and the dissenting opinion of Judge Philips in *Edelstein v. U. S.*, 17 Am. B. R. 649, 149 Fed. 636, * * *, which are directly in point and fully sustain his contention. He also cites dicta in *Re Marx* (D. C.), 4 Am. B. R. 521, 102 Fed. 676, and in *Re Logan* (D. C.), 4 Am. B. R. 525, 102 Fed. 876; in *Re Leslie* (D. C.), 9 Am. B. R. 561, 119 Fed. 406; in *Re Dow's Estate* (D. C.), 5 Am. B. R. 400, 105 Fed. 889, and in *Re Gaylord*, 7 Am. B. R. 1, 112 Fed. 668, 50 C. C. A. 415. On the other hand, the provision quoted was held not to give immunity from prosecution for giving false testimony upon an examination under the Bankruptcy Act in a well-considered opinion concurred in by a majority of the court in *Edelstein v. U. S.*, 17 Am. B. R. 649, 149 Fed. 636, * * * (C. C. A.); and an application for certiorari in that cause was refused by the Supreme Court (205 U. S. 543). * * * Whatever might be our conclusions were the question presented as a novel one, we are clearly of the opinion that we should follow the construction adopted in the Eighth Circuit and left undisturbed by the Supreme Court, so that in a matter of so much importance the decisions of the Federal courts in the different circuits may be uniform."

Section 860 of the United States Revised Statutes has been repealed since the decision of *Wechsler v. United States*.⁷⁴

§ 1556½. But Such Immunity Is Not a Bar to Prosecution for Perjury Committed by Bankrupt When Examined under § 7 (9).—For a long time it was doubted whether this immunity did not create an effective obstacle to any conviction for perjury in swearing falsely before the referee, some courts holding the provision granted immunity from prosecution for the falseness of the testimony itself,⁷⁵ while other courts held it extended simply to prosecution for any actual crime revealed by the testimony.⁷⁶

However, the matter has been definitely set at rest by the Supreme Court of the United States, to the effect that the immunity afforded by § 7 (9) is not applicable to a prosecution for perjury committed by the bankrupt when examined under that subdivision of § 7.⁷⁷

⁷⁴ See post, § 2324½.

⁷⁵ *United States v. Simon*, 17 A. B. R. 41, 146 Fed. 89 (D. C. Wash.); *In re Marx*, 4 A. B. R. 521, 102 Fed. 676 (D. C. Ky.); *In re Logan*, 4 A. B. R. 525, 102 Fed. 876 (D. C. Ky.); *In re Leslie*, 9 A. B. R. 561, 119 Fed. 406; *In re Dow's Estate*, 5 A. B. R. 400, 105

Fed. 889; *In re Gaylord*, 7 A. B. R. 1, 112 Fed. 668, 50 C. C. A. 415.

⁷⁶ *Wechsler v. United States*, 19 A. B. R. 1, 158 Fed. 579 (C. C. A. N. Y.); *United States v. Brod*, 2 A. B. R. 740, 176 Fed. 165 (D. C. Ga.).

⁷⁷ See *Daniels v. United States*, 27 A. B. R. 790 (C. C. A. Ohio), decided since *Glickstein v. United States*.

Glickstein v. United States, 222 U. S. 139, 27 A. B. R. 786: "When the legality of a conviction and sentence of Glickstein was before the court below, as the result of error prosecuted by him, the court, stating the facts which we have recited, certified the following question: 'Is subsection 9 and the immunity afforded by it applicable to a prosecution for perjury committed by the bankrupt when examined under it?' * * * "With these propositions in hand, it follows that the precise question for decision is, Did the guaranty of immunity contained in the 9th subdivision of § 7 of the Bankruptcy Act bar a prosecution for perjury for false swearing in giving testimony under the command of the section? In other words, the sole question is, Does the statute, in compelling the giving of testimony, confer an immunity wider than that guaranteed by the Constitution? The argument to maintain that it does is that, as the statute provides for immunity, and does not contain the reservation found in either Rev. Stat., § 860, or that embodied in the Act of 1893, therefore, under the rule that the inclusion of one is the exclusion of the other, such a reservation cannot be implied. Or, to state the proposition in another form, it is that as the statute in the immunity clause says: 'But no testimony given by him (the witness who is compelled to be examined) shall be offered in evidence against him in any criminal proceeding,' and as these words are unambiguous, there is no room for limiting the language so as to cause the immunity provision not to prohibit the offer of the testimony in a criminal prosecution for perjury. But the contention assumes the question for decision, since it excludes the possibility of construction when, on the face of the statute, the meaning attributed to the immunity clause cannot be given to it without destroying the words of the statute and frustrating its obvious object and intent. This may not be denied, since the statute expressly commands the giving of testimony, and its manifest purpose is to secure truthful testimony, while the limited and exclusive meaning which the contention attributes to the immunity clause would cause the section to be a mere license to commit perjury, and hence not to command the giving of testimony in the true sense of the word. The argument that because the section does not contain an expression of the reservation of a right to prosecute for perjury in harmony with the reservations in Rev. Stat., § 860, and the Act of 1893, therefore it is to be presumed that it was intended that no such right should exist, we think, simply begs the question for decision, since it is impossible in reason to conceive that Congress commanded the giving of testimony, and at the same time intended that false testimony might be given with impunity, in the absence of the most express and specific command to that effect.

Bearing in mind the subject dealt with, we think the reservation of the right to prosecute for perjury, made in the statutes to which we have referred, was but the manifestation of abundant caution; and hence, the absence of such reservation in the statute under consideration may not be taken as indicative of an intention on the part of Congress that perjury might be committed at pleasure. Some of the considerations which we have pointed out were accurately expounded in *Edelstein v. United States*, 17 Am. B. R. 649, 149 Fed. 636, 9 L. R. A. (N. S.) 236, 79 C. C. A. 328, by the Circuit Court of Appeals for the eighth circuit, and in *Wechsler v. United States*, 19 Am. B. R. 1, 158 Fed. 579, 86 C. C. A. 37, by the Circuit Court of Appeals for the second circuit, and this leads us to observe that the necessary result of the conclusion now reached is to disapprove the opinions in *Re Marz* (D. C. Ky.) 4 Am. B. R. 521, 102 Fed. 676, and *Re Logan* (D. C. Ky.), 4 Am. B. R. 525, 102 Fed. 876. It follows that the question propounded must receive a negative answer, and our order will be, question certified answered 'No.'

Edelstein v. U. S., 17 A. B. R. 658, 149 Fed. 636 (C. C. A. Minn.): "The government contends that the immunity has sole reference to the use of evidence in a

prosecution for some offense to which his evidence related: that Congress offered as an inducement to a full, frank, and truthful disclosure by a bankrupt for the benefit of his creditors of all matters and things concerning his property and estate that his evidence should not be used against him in any prosecution for any such offense, however much it might implicate him. Defendant's argument is that the language employed is comprehensive and unequivocal; 'that no testimony given by him shall be offered against him in any criminal proceeding;' that it, in terms, prohibits the use of the negative answer given by the bankrupt to the question propounded to him, although knowingly and intentionally false, as a basis for the criminal charge involved in the indictment now under consideration. To this we cannot give our assent. There is no rule requiring a literal construction to be placed even upon unambiguous words of a particular clause of a statute without consideration of its context. The meaning of specific words in one part of a statute is often controlled by other provisions of the same act, and frequently by provisions of other acts which are in *pari materia*. * * * Moreover, it would, in effect, secure to the bankrupt the immunity in question for violating his part of the compact, namely, to testify—that is, to testify truthfully—by virtue of which he secured a right to the immunity. We are not willing to impute to Congress any such contradictory and absurd purpose. The words 'any criminal proceeding' cannot sensibly or reasonably be construed so literally and generally as to include the criminal proceeding provided by law for false swearing in giving his testimony.'"

§ 1557. Whether Protection Applies Only to Federal Prosecution.

—It is a question whether the protection afforded by § 7 (9) of the Bankrupt Act applies only to proceedings in the federal courts,⁷⁸ or whether it also extends to those in the state courts. However, inasmuch as § 7 (9) has been held not to prohibit the use of the bankrupt's schedules,⁷⁹ nor of the books, papers and documents of the bankrupt passing to the trustee by operation of § 70 (a) (1) but is confined solely to testimony given while under examination authorized by § 7 (9) and § 21 (a), the question does not properly arise when the evidence offered to be introduced is the bankrupt's schedules, books, etc.⁸⁰

Ensign v. Commonwealth of Pa., 227 U. S. 592, 30 A. B. R. 408: "For the reasons given, it seems to us clear that the plaintiffs in error were not entitled to have the bankruptcy schedules excluded from evidence, because those schedules were not within the description of 'testimony' in the clause quoted from § 7 of the Bankruptcy Act. And for like reasons, the evidence showing the results of an expert examination of the books of the bankers was also admissible. This conclusion renders it unnecessary for us to consider whether the prohibition with which we have dealt, that 'no testimony given by him shall be offered in evidence against him in any criminal proceeding,' is not limited to criminal proceedings in the Federal courts; and upon this question we express no opinion."

On the other hand, where the evidence sought to be introduced against the bankrupt in the state court is testimony given while under the examination authorized by §§ 7 (9) and 21 (a) of the Bankruptcy Act, the ques-

⁷⁸ *Ensign v. Commonwealth of Pa.*, 227 U. S. 592, 30 A. B. R. 408.

⁸⁰ *In re Hess*, 14 A. B. R. 562, 134 Fed. 109 (D. C. Pa.).

⁷⁹ *Ensign v. Commonwealth of Pa.*, 227 U. S. 592, 30 A. B. R. 408.

tion becomes important. And it has been held in one case that, since this is a matter of procedure, the prohibition would not be binding upon the state court.⁸¹

In *re Nachman*, 8 A. B. R. 181, 182, 114 Fed. 995 (D. C. S. C.): "The provision can have no other effect than to protect him against the use of his testimony in any prosecution in the courts of the United States. It would be no answer to a prosecution which might be instituted in the state courts, which are not created by acts of Congress, and which prescribe their own rules of proceedings independently of Congress."

Evidence taken in the bankrupt's examination may be used against him on the hearing of objections to his discharge: opposition to discharge not being a criminal proceedings, even though a crime be charged.⁸² Also it may be used on hearings upon petitions for orders upon bankrupts to surrender assets claimed to be in their possession,⁸³ and in similar proceedings.

§ 1558. Incriminating Questions—Constitutional Rights Preserved, Notwithstanding § 7 (9).—The constitutional right of a witness granted by the Fifth Amendment to the Federal Constitution, to refuse to answer questions and produce documents or other evidence that in his estimation would tend to incriminate him, is preserved, both as to bankrupts and as to all other witnesses; and this is so notwithstanding that, as to the bankrupt, under § 7 (9), no testimony given by him may be offered in evidence against him in any criminal proceedings, this statutory protection of the bankrupt from the use of such testimony not being as broad as his constitutional privilege to refrain from giving it altogether.⁸⁴ Thus, as to the bankrupt, it is preserved.⁸⁵

⁸¹. *Contra*, obiter, *United States v. Goldstein*, 12 A. B. R. 157, 132 Fed. 789 (D. C. Va.).

⁸². In *re Woodford Gaylord*, 7 A. B. R. 1, 112 Fed. 668 (C. C. A. N. Y.), affirming 5 A. B. R. 410; In *re Dow*, 5 A. B. R. 400, 105 Fed. 889 (D. C. Iowa). *Contra*, In *re Marx*, 4 A. B. R. 521, 102 Fed. 676, disapproved in *In re Gaylord*, 7 A. B. R. 1, and also disapproved in *In re Dow*, 5 A. B. R. 400, 105 Fed. 889 (D. C. Iowa).

⁸³. In *re Alphin & Lake Cotton Co.*, 12 A. B. R. 653, 131 Fed. 824 (D. C. Ark.).

⁸⁴. U. S. Const., Amend. V. In *re Tracy & Co.*, 23 A. B. R. 438, 177 Fed. 332 (D. C. N. Y.).

Bankrupt's deposition not suppressed because of refusal to answer on ground of tending to incriminate. Compare, *Carey v. Donohue*, 31 A. B. R. 210, 209 Fed. 328 (C. C. A. Ohio).

⁸⁵. Compare, *Counselman v. Hitchcock*, 142 U. S. 547 (distinguished in *Burrell v. State*, 12 A. B. R. 132, 194

U. S. 572); compare, *Brown v. Walker*, 161 U. S. 591.

In *re Glassner, Snyder & Co.*, 8 A. B. R. 184 (Ref. Md.): In this case the bankrupt made a general plea to a petition for an order requiring him to surrender certain assets and certain books and documents that he should not be required to answer thereto because such answer might tend to subject him to punishment.

In *re Feldstein*, 4 A. B. R. 321, 103 Fed. 269 (D. C. N. Y.); In *re Kanter and Cohen*, 9 A. B. R. 104 (D. C. N. Y.); In *re Henschel*, 7 A. B. R. 207 (Ref. N. Y.); In *re Shera*, 7 A. B. R. 552, 114 Fed. 207 (D. C. N. Y.); *United States v. Goldstein*, 12 A. B. R. 755, 132 Fed. 789 (D. C. Va.); In *re Scott*, 1 A. B. R. 49, 95 Fed. 815 (D. C. Penn.); obiter, *United States v. Simon*, 17 A. B. R. 46, 146 Fed. 89 (D. C. Wash.); obiter, In *re Hess*, 14 A. B. R. 562, 563, 134 Fed. 109 (D. C. Wash.); In *re Hawthorn*, 2 A. B. R. 298 (Ref. La.); *contra*, *Mackel v. Rochester*, 4 A. B. R. 1, 102 Fed. 314 (C. C. A.

In re Rosser, 2 A. B. R. 755 (D. C. Mo.): "To compel him to answer the question is a violation of rights guaranteed to him by the fifth amendment to the constitution. * * *

"It was urged in argument that he could not avail himself of this provision of the constitution, because, under the seventh section of the Bankrupt Law, it is expressly provided, 'but no testimony' given by him shall be offered in evidence against him in any criminal proceeding.' But this language is not half so strong nor half so broad as the language of the Act of February 25, 1868 (15 Stat. 37), which was considered, and the same argument made in the case of Counselman v. Hitchcock, 142 U. S. 560, in which case the court held that the witness could not be compelled to answer."

In re Walsh, 4 A. B. R. 693, 104 Fed. 518 (D. C. S. Dak.): "Now, while it is very desirable, as the Court of Appeals in the Ninth Circuit says, that the bankrupts should be compelled to answer these questions, so that the estate of the bankrupt should be properly administered and distributed, still the bankruptcy law, and the courts, and all of us are bound by the superior provisions and paramount authority of the Constitution of the United States, and all and everything must give way to its mandates. I can see that in some instances the fact that the bankrupt stands upon his constitutional guaranty would interfere with the proper administration of the bankruptcy law, but that is not a question which the court has the power to remedy."

In re Nachman, 8 A. B. R. 182, 183, 114 Fed. 995 (D. C. S. C.): "Testimony thus given under compulsion might be used to search out other testimony which could be used against him, a clue to which might not otherwise be obtained, and the immunity provided by the constitution would thus be frittered away. No act of Congress can deprive a citizen of the privileges afforded by the constitution unless it supplies a complete protection from all perils against which the constitution was intended to provide. Section 7 of the Bankrupt Act, cited above, does not provide such complete protection. * * * It may be well contended that the object designed to be accomplished by § 7 of the Bankrupt Act, which requires the bankrupt to submit to an examination concerning the conduct of his business, will be defeated, if the witness is thus permitted to refuse to testify concerning his dealings with his creditors and others, and such undoubtedly is the unfortunate result; but it is for the Congress to provide, if it can, against such contingencies. It might well provide that a witness who refused to answer questions concerning his business should be deprived of his right to a discharge. That would be within its right. The courts cannot deprive a citizen of the constitutional right invoked by him for his protection upon any consideration of inconvenience or for the purpose of administering what it may regard as a salutary and useful law.

"My conclusion, therefore, is that a witness, under examination before a referee in bankruptcy, cannot be compelled to answer a question the answer to which he claims will tend to criminate him."

Thus, as to other witnesses it is likewise preserved.^{85a} And the protec-

Mont.); contra, In re Franklin Syndicate, 4 A. B. R. 511, 114 Fed. 205 (D. C. N. Y.), distinguished in In re Shera, 7 A. B. R. 552, 114 Fed. 207 (D. C. N. Y.); obiter, Edelstein v. United States, 17 A. B. R. 658 (C. C. A. Minn.); In re Harris, 20 A. B. R. 911, 164 Fed. 292 (D. C. N. Y.); In re Tracy & Co., 23 A. B. R. 438, 177 Fed. 532 (D. C. N. Y.).

^{85a}. In re Feldstein, 4 A. B. R. 321, 103 Fed. 269 (D. C. N. Y.).

In re Smith, 7 A. B. R. 213, 112 Fed. 509 (D. C. N. Y.): In this case the court held, that a trustee in bankruptcy could not be compelled to give testimony which might tend to show he had misappropriated the funds of the bankrupt estate.

In re Smelting Co., 15 A. B. R. 83,

tion extends to the production of documents, as well as to the giving of testimony.⁸⁶

Boyd v. U. S., 116 U. S. 616: "The compulsory production of a man's private papers to be used in evidence against him is equivalent to compelling him to be a witness against himself in a prosecution for a crime, penalty or forfeiture, and is equally within the prohibition of the Fifth amendment."

Likewise, the bankrupt may omit from his schedules answers to questions therein which might tend to incriminate him.

In *re Podolin*, 30 A. B. R. 576, 205 Fed. 563 (D. C. Pa. affirmed, *Podolin v. Warner Dry Goods Co.*, 31 A. B. R. 796, 210 Fed. 97, C. C. A. Pa.): "The referee's order of May 12, 1913, will be so modified as to provide expressly that the bankrupts may omit from their schedules any reference to the transaction with Rudsky. They are still exposed to the danger of prosecution in connection with that transaction, and they should not be compelled to run the not remote risk of having their statements used against them in such a prosecution. The connection between such statements and the evidence required to sustain the prosecution is direct and immediate."

And it is not essential that a prosecution be actually pending.

In *re Hess*, 14 A. B. R. 562, 134 Fed. 109 (D. C. Wash.): "The fact that no prosecution is now pending against the bankrupt is no answer to his right to claim this constitutional privilege. The meaning of the constitutional provision is not simply that he shall not be compelled to produce books and papers which may contain evidence tending to incriminate him in a pending prosecution for a criminal offense against him, but its object is to insure him against such compulsory production of his books and papers containing incriminating evidence in any proceeding or investigation, whether such compulsory disclosure is sought directly to establish his guilt, or indirectly and incidentally for the purpose of proving facts involved in an issue between other parties. If the disclosure thus made would be capable of being used against him as a confession of crime, or an admission of facts tending to prove the commission of an offense by himself, in any prosecution then pending, or that might be brought against him thereafter, such disclosure would be an accusation of himself, within the meaning of the constitutional provision."

Impliedly, In *re Sapiro*, 1 A. B. R. 296, 92 Fed. 340 (D. C. Wis.): "But the privilege is asserted here in favor of the bankrupt to excuse him from producing the books of account kept in the business which he was conducting when his voluntary petition was filed to invoke the benefits and submit to the requirements of the Bankruptcy Law. He thereby elected to place all his property (aside from exemptions) including these books of account which contain ap-

138 Fed. 954 (D. C. Penn.), where an officer of a bankrupt corporation under indictment for embezzlement of its funds refused to testify whether he had taken any part of the bankrupt's property but was required to testify whether he had then any of its money or property in his possession.

⁸⁶ In *re Hess*, 14 A. B. R. 562, 563, 134 Fed. 109 (D. C. Wash.); In *re Kanter & Cohen*, 9 A. B. R. 104, 117 Fed. 356 (D. C. N. Y.); In *re Glass-*

ner, Snyder & Co., 8 A. B. R. 184 (Ref. Md.); impliedly, In *re Rosenblatt*, 10 A. B. R. 308, 143 Fed. 663 (D. C. Penn.); apparently, contra, *People v. Swarts*, 8 A. B. R. 490 (Criminal Court Cook Co. Ills.).

In *re Harris*, 20 A. B. R. 911, 164 Fed. 292 (D. C. N. Y.), where the books contained entries showing the falsity of statements to a commercial agency; In *re Tracy & Co.*, 23 A. B. R. 438, 177 Fed. 532 (D. C. N. Y.).

parently the only evidence of credits outstanding at the disposition of this court. If he were otherwise privileged to withhold the books his petition operates both as a waiver and as a transfer of the right of custody and the books cannot now be withheld or withdrawn upon the assertion that they may contain incriminating evidence or matter."

While the constitutional privilege, granted by the Fifth Amendment to the Federal Constitution, is not obligatory upon the state courts since it regulates merely the procedure in the federal courts,⁸⁷ yet, if the disclosure sought to be obtained in the federal court could be used against the bankrupt in a state court prosecution, he may still claim the privilege to refuse to answer, even though he is granted immunity by statute from the use of the testimony in a federal prosecution. The immunity would have to be as broad as his constitutional privilege and extend to the use of his testimony in the state court, to avoid the privilege.⁸⁸

However, it has been held that where the bankrupt has once voluntarily delivered to the federal court, books, documents and papers, the trustee will not be restrained from offering them to the prosecuting authorities of a state.⁸⁹

And the books of the bankrupt which have been surrendered to the trustee, although unwillingly, also may be produced before the grand jury and before the petit jury at the trial, because such use of documentary evidence is not "compelling" the defendant to be a witness against himself.^{89a}

Johnson v. U. S., 227 U. S. 600, 30 A. B. R. 14: "On the first point the facts are simply that the books had been transferred to the trustee in accordance with § 70 of the Bankruptcy Act, and were produced before the grand jury and before the petit jury at the trial. That the transfer lawfully could be required is established by *Re Harris*, 221 U. S. 274, 26 A. B. R. 302. But the defendant lays hold of an expression in that case, 'the properly careful provision to protect him from use of the books in aid of prosecution,' as an intimation that the books could not be put to such a use.

"Courts proceed step by step. And we now have to consider whether the cautious statement in the former case marked the limit of the law in a case where

⁸⁷. *Ensign v. Commonwealth of Pa.*, 227 U. S. 530, 30 A. B. R. 408.

⁸⁸. *In re Hess*, 14 A. B. R. 562, 563, 134 Fed. 109 (D. C. Wash.). Compare ante, § 1557.

And the rule has been extended, though in a case of doubtful authority, even to cases where books of a bankrupt corporation seized by its receiver, in bankruptcy are sought to be used in a criminal prosecution against the president and one of the employees of the company, the court holding that although the secretary was the proper immediate custodian of corporate books, yet the president theoretically was also custodian. *People v. Swarts & Greenberg*, 8 A. B. R. 490 (Criminal Court Cook Co. Ills.); *S. C.*, 24 Nat'l Corp.

Rep. 262: "The court would hold that they were as much in his possession, so far as the right of production is concerned, and the power of production, as they were in the hands of the secretary. If that be true, then these books were taken from the possession of the president of this company and of the secretary, and I am obliged to hold that the contents of these books would be incompetent evidence."

⁸⁹. *Ensign v. Commonwealth of Pa.*, 227 U. S. 530, 30 A. B. R. 408; *In re Tracy & Co.*, 23 A. B. R. 438, 177 Fed. 532 (D. C. N. Y.), quoted at § 1561.

^{89a}. But compare, inferentially contra, obiter, *In re Tracy & Co.*, 23 A. B. R. 438, 177 Fed. 532 (D. C. N. Y.).

no rights, if there were any, were saved when the books were transferred. The answer was implied in that decision. A party is privileged from producing the evidence, but not from its production. The transfer by bankruptcy is no different from a transfer by execution of a volume with a confession written on the fly leaf. It is held that a criminal cannot protect himself by getting the legal title to corporate books. *Wheeler v. United States*, 226 U. S. 478. But the converse proposition is by no means true, that he may keep the protection from the introduction of documentary evidence that he would have had while he retained it, after the title and possession have gone to someone else.

"It is true that the transfer of the books may have been against the defendant's will, but it is compelled by the law as a necessary incident to the distribution of his property, not in order to obtain criminal evidence against him. Of course, a man cannot protect his property from being used to pay his debts by attaching to it a disclosure of crime. If the documentary confession comes to a third hand *alio intuitu*, as this did, the use of it in court does not compel the defendant to be a witness against himself."

The privilege may not be asserted so as to prevent the production and surrender to the trustee of those documents, books, deeds and instruments in writing, relating to the bankrupt's business, the actual title to which passes to the trustee by operation of law under § 70 (a) (1) as defined by § 1 (13).⁹⁰

In *re Harris*, 221 U. S. 274, 26 A. B. R. 302: "The question is not of testimony but of surrender—not of compelling the bankrupt to be a witness against himself in a criminal case, present or future, but of compelling him to yield possession of property that he no longer is entitled to keep. If a trustee had been appointed, the title to the books would have vested in him by the express terms of section 70, and the bankrupt could not have withheld possession of what he no longer owned, on the ground that otherwise he might be punished. That is one of the misfortunes of bankruptcy if it follows crime. The right not to be compelled to be a witness against oneself is not a right to appropriate property that may tell one's story."

United States v. Halstead, 27 A. B. R. 302, 195 Fed. 295 (D. C. Ill.): "If the order had been to produce the books in a criminal investigation pending before the grand jury and they contained matter that might incriminate himself, he would have come under the protection of the fifth amendment, and nothing short of statutory immunity would then suffice. But the order was to deliver them as property, the title to which was passed from him, and if, as an incident of that change of possession they should come to be used as evidence in a criminal prosecution, it is one of the misfortunes of bankruptcy. As was said: 'The right not to be compelled to be a witness against one's self is not a right to appropriate property that may tell one's story.'"

And surrender to a receiver may be enforced because the right to enforce title in the trustee later appointed carries with it the right to enforce surrender of possession to the receiver in the meantime.

In *re Harris*, 221 U. S. 274, 26 A. B. R. 302: "As the bankruptcy court could

⁹⁰. Impliedly and obiter, *Kerrch v. United States*, 22 A. B. R. 544, 171 Fed. 366 (C. C. A. Mass.). Compare, In *re Harris*, 20 A. B. R. 911, 164 Fed. 292

(D. C. N. Y.), where this principle apparently was applicable, but was not adverted to.

have enforced title in favor of the trustee, it could enforce possession *ad interim* in favor of the receiver."

Nor may the privilege be asserted to prevent the introduction into evidence of the bankrupt's books of account and papers already in the possession of the trustee or receiver.⁹¹

It has been held that the use of the bankrupt's books and papers violates neither the Fourth nor Fifth Amendment to the Federal Constitution.⁹²

§ 1559. Where Answer by No Reasonable Possibility Could Tend to Incriminate, No Privilege.—But where the answer to a question cannot by any reasonable possibility tend to incriminate him, the bankrupt or witness, he must answer.⁹³

Brown v. Walker, 161 U. S. 599: "The object of the law is to afford to a party, called upon to give evidence in a proceeding *inter alios*, protection against being brought by means of his own evidence within the penalties of the law. But it would be to convert a salutary protection into a means of abuse if it were to be held that a mere imaginary possibility of danger, however remote and improbable, was sufficient to justify the withholding of evidence essential to the ends of justice."

In *re Levin*, 11 A. B. R. 382, 131 Fed. 388 (D. C. N. Y.): "As I understand the rule, if the question is of such a description that the answer may or may not criminate the witness, he can refuse to answer (Judge Marshal's opinion on Burr trial). But if the court is convinced that the answer to the question cannot by any possibility criminate him and especially if the witness does not swear that he believes it would, it is the duty of the court to compel him to answer. Otherwise every bankrupt can absolutely refuse to be examined at all." The syllabus in this case is: "A bankrupt under examination may be punished as for contempt for refusing to answer question: (1) As to the accuracy of a creditor's proof of claim; (2) as to whether or not the signature to notes held by a creditor were his; (3) Whether or not he knew a particular creditor who had filed a claim, and whether or not he was a salesman in his employ; (4) as to the identity of his check book after testifying that he could tell whether or not a check has been paid by reference to each of his checks; as each of the questions could not, by any of the questions asked, tend to degrade or incriminate him."

Obiter, In *re Kantor & Cohen*, 9 A. B. R. 104, 117 Fed. 356 (D. C. N. Y.): "In a case where it clearly appears to the court that a party from whom evidence is sought contumaciously or mistakenly refuses to furnish that which cannot possibly injure him, he will not be permitted to shield himself behind the privilege, but generally the party best knows what he cannot furnish without accusing himself and where it is not perfectly evident and manifest that the evidence called for will not be incriminating, the privilege must be allowed."

In *re Hess*, 14 A. B. R. 826, 134 Fed. 109 (D. C. Pa.): "But who is to be the judge whether or not the books and papers do actually contain evidence of an incriminating nature, as alleged by the bankrupt? Can it be that upon the filing of an involuntary petition in bankruptcy, the bankrupt can refuse to deliver possession of the books and papers to the trustee, when called upon to do

91. *Kerrch v. United States*, 22 A. B. R. 544, 171 Fed. 366 (C. C. A. Mass.).

92. *United States v. Halstead*, 27 A. B. R. 302 (Ct. App. Dist. Columbia).

93. In *re Franklin Syndicate*, 4 A. B. R. 511, 114 Fed. 205 (D. C. N. Y.). Compare, inferentially, In *re Hark Bros.*, 14 A. B. R. 625 (D. C. Penn.).

so, by answering that they contain incriminating evidence? He may desire to retain possession of his books for the purpose of concealing assets, or he may honestly be mistaken as to the effect of the evidence alleged to be incriminating; the transactions, which, in his judgment, are incriminating, may not be acts or transactions of an incriminating nature, and, if established, may not constitute an offense; the Statute of Limitations may bar a prosecution. All these matters should be considered in passing upon the question as to whether or not the books do contain evidence of an incriminating nature.

"When a witness is before the court in a proceeding, and a question is propounded, it must appear to the court, from the circumstances of the case and the nature of the evidence which the witness is called to give, that there is reasonable ground to apprehend danger to the witness from being compelled to answer, to entitle him to the privilege of silence, and where the fact of the witness being in danger be once made apparent to the court, great latitude should be allowed to him in judging for himself of the effect of any particular question. * * *

"This being the practice when witnesses are called to testify and claim their privilege, it is equally important, under the Bankrupt Law, that the Court should pass upon the probability of danger to the bankrupt when he pleads his constitutional privilege, upon a demand made by a trustee in bankruptcy for him to deliver his books and papers, as required by that Act."

In *re Rosenblatt*, 16 A. B. R. 308, 143 Fed. 663 (D. C. Pa.): "It is contended that the bankrupts are the sole judges of that question, and they are not required to do more than to claim their constitutional privilege that they are the sole judges of the question as to whether or not the books do contain such evidence, and that they are not required in any manner, by the production of evidence, to satisfy the court that their claim has some foundation in fact. If this be the law, then, bankrupts in every case can retain their books, and creditors will be unable to secure evidence of what in most mercantile concerns is the most valuable asset, to-wit: The book accounts. It would be the greatest possible encouragement to dishonest debtors to practice frauds upon their creditors and then destroy the evidence of it. But this question has been settled by the courts. They have taken a more reasonable view, which requires that it shall appear to the court that the claim is made in good faith and that there is reasonable ground to apprehend danger from the production of the books, and when this fact does appear then great latitude should be allowed the claimant in judgment for himself as to the effect of any particular question or production of a book. 'But it would be to convert a salutary protection into a means of abuse if it were to be held that a mere imaginary possibility of danger, however remote and improbable, was sufficient to justify the withholding of evidence essential to the ends of justice.' *Brown v. Walker*, 161 U. S. 599. And it would be equally potential in converting a salutary protection into a means of abuse if a bankrupt were permitted to judge entirely for himself, regardless of the facts, whether or not the production of a book will tend to incriminate him."

Obiter, In *re Walsh*, 4 A. B. R. 693, 696, 104 Fed. 518 (D. C. S. Dak.): "And in questions where the referee is satisfied clearly that the bankrupt would not criminate himself by answering the same, he would not be entitled to the protection."

Inferentially and obiter, In *re Nachman*, 8 A. B. R. 183, 114 Fed. 905 (D. C. S. C.): "Under the provisions of § 7, the witness is compelled to give testimony concerning his business, and he cannot interpose objections which will shut out all light whatever from his creditors. The constitutional immunity can only be invoked to protect him from answering a question the answer to

which might subject him to prosecution. In the further conduct of the examination the referee is directed, whenever a question is propounded, to notify the witness that he is not required to answer it if the answer would tend to criminate himself. It is only questions of that nature that he may refuse to answer. He is not to be permitted to interpose his constitutional immunity as a shield to every inquiry concerning his business, nor is his counsel to be permitted to delay or obstruct inquiry by making objections for him."

In *re Bendheim*, 24 A. B. R. 254 (D. C. N. Y.): "Undoubtedly it is always a difficult thing to say at just what point a bankrupt who is compelled to answer, and who claims his privilege, should be allowed the exercise of his own unquestioned judgment of the danger of self-incrimination. A priori no question can be said to be outside of the range of proof of some crime, and to allow him to stand mute in all cases is to give him the privilege of keeping silent as to all his affairs, in the interest of merely pedantic and verbal integrity of principle. While in all cases he must be given the benefit of all doubts, there must be something which gives rise to a probability of damage upon which a doubt may be based. *Queen v. Boyes*, 1 B. & S. 311, 321. * * * But in the absence of some claim on his part coupled with some proof of reasonable expectation that that claim has a basis, his danger is in my judgment purely academic."

And the same qualification applies to the right to omit from schedules reference to certain transactions.

In *re Podolin*, 30 A. B. R. 576, 205 Fed. 563 (D. C. Pa., affirmed, *Podolin v. Warner Dry Goods Co.*, 31 A. B. R. 796, 210 Fed. 97, C. C. A. Pa.) [quoted also at § 1558]: "But their objection to filling out the other schedules cannot be sustained. These (A3, A4, B2C, and B3a) require them to set forth certain facts about their financial condition in October, and I have not been convinced that these facts have so close a connection with the written representations about their condition that were mailed in the preceding June as would tend to convict them of a postal crime in making such representations. In my opinion the connection, if it exists at all, is remote and contingent, and need not be taken into account."

However, even where the answers might perhaps be inculpatory yet the bankrupt may not refuse altogether to file schedules, but must make a bona fide effort to comply with the provisions of the Act, without incriminating himself.

In *re Podolin*, 29 A. B. R. 406, 202 Fed. 1014 (D. C. Pa., affirmed sub nom, *Podolin v. Warner Dry Goods Co.*, 31 A. B. R. 796, 210 Fed. 97, C. C. A. Pa.): "As a general proposition, the referee's ruling that the bankrupts must file schedules, so far as they can do so without incriminating themselves, is obviously correct. But until an effort is made to comply with his order, it is practically impossible for the court to decide whether a particular fact is to be included or omitted. To decide that a bankrupt is not bound to put his hand to a declaration of fact that may incriminate him, does not advance a particular dispute very much; what is required is an effort in good faith by the bankrupt to file a schedule that obeys the Act up to the point where the court can see that further obedience would violate the constitutional protection. When the bankrupts present such schedules as they can conscientiously declare to be a compliance with the order (saving their constitutional rights) the referee will then be able, either to order them to do specific acts or to approve the refusal to do them; and in either event the District Court will then have something definite to rule upon. Until such a situation is presented, the discussion is almost wholly academic."

And he must set forth in his schedules that he refuses to answer the query because of danger of incrimination: mere silence is not enough.

§ 1560. Privilege Does Not Authorize Refusal to Be Sworn Altogether nor to Produce Documents nor to File Schedules.—And the privilege does not authorize a bankrupt to refuse altogether to be sworn, nor to refuse altogether to produce the documents or books, but simply to refuse to answer questions as they are put or to allow inspection of the particular document or pages of the book as they are called for: the bankrupt must be sworn and the books or documents must be produced.⁹⁴

In re Hark Bros., 14 A. B. R. 624, 136 Fed. 986 (D. C. Pa.): "The order to produce them before him should have been complied with, and then the question as to whether this plea of the bankrupts is well founded could be determined by the referee."

In re Hess, 14 A. B. R. 563, 564, 134 Fed. 109 (D. C. Pa.): "Where, under these circumstances, a bankrupt pleads this privilege, he should be required to bring the books and papers, which he alleges contain the incriminating evidence, before either the court or referee in bankruptcy, and when it is made to appear that his plea is well founded, the court can make such order in the case as will fully protect him from discovery of such evidence, and, at the same time, if possible, enable the trustee to obtain such information from the books as is always necessary and indispensable in the settlement of bankrupt estates."

Compare, even stronger rule, In re Harris, 20 A. B. R. 911, 164 Fed. 292 (D. C. N. Y.): "A rule under which a bankrupt may, in any case, at his own option, refuse to produce his books may, in many instances, almost paralyze the power of the court to administer the estate. No business of any considerable magnitude can be or is carried on without keeping books of account; and when such a business becomes bankrupt it is practically almost impossible for a receiver or trustee to properly discharge his duties without having possession of the books of the business. In view of this necessity in bankruptcy cases it has been held that a bankrupt is not permitted to withhold his books from his trustee on his mere assertion that they tend to incriminate him, but must produce them before the court or referee in bankruptcy in order to have the question determined whether they do, in fact, tend to incriminate him; and that, if it appears that they do contain incriminating evidence, the court can make such an order as will protect the bankrupt from the use of such evidence for any criminal proceeding, and at the same time will enable the trustee to make such use of the books as may be necessary to administer the estate."

Nor, as we have seen in the preceding section, will it permit the bankrupt to refuse altogether to file schedules: he must not only file the schedules but

⁹⁴. As to books, see decision of District Court embodied in opinion of C. C. A. in *Goodman v. Brenner*, 6 A. B. R. 470, 109 Fed. 481 (C. C. A. La.); In re Rosenblatt, 16 A. B. R. 308, 143 Fed. 663 (D. C. Penn.).

No appeal lies from such ruling, it being simply an interlocutory order and not a final order, *Goodman v.*

Brenner, 6 A. B. R. 470, 109 Fed. 663 (D. C. Penn.).

The bankrupt is not permitted to qualify his oath: the constitutional guaranty protects him without express reservation, In re Scott, 1 A. B. R. 49, 95 Fed. 815 (D. C. Pa.).

Compare, In re Podolin, 29 A. B. R. 408, 202 Fed. 1014 (D. C. Pa.), quoted on other points at §§ 1558, 1559.

must state therein that the reason he omits the particular item is that its answer would tend to incriminate him.^{94a}

§ 1561. Privilege to Be Claimed at Time Question Asked or Production Demanded.—The time to claim the privilege is when the question is asked, and, if not then claimed, it is waived.⁹⁵

Burrell v. State, 194 U. S. 572, 12 A. B. R. 132: "The statute does not prohibit the use of testimony against the consent of him who gave it. It prescribes a rule of competency of evidence which may or may not be insisted upon. It does not declare a policy of protection of which cannot be waived. And the time to avail of it is when the testimony is offered. After the testimony is admitted, its probative force cannot be limited. This could not be contended even under the broader provision of the Constitution. A witness who voluntarily testifies cannot resist the effect of the testimony by claiming that he was not compellable to give it.

"In the case at bar, the court dealt with testimony which had been admitted without question or objection. * * *

"In the case at bar, as we have already said, plaintiff in error did not claim the protection afforded him by the Bankrupt Act. He made no objection to the use of the testimony which he gave before the referee, nor does he now urge its use as error. He broadly claimed, and now claims, exemption from prosecution. For the reasons we have given the claim is untenable."

And when the book or document is about to be inspected.⁹⁶

The privilege should be claimed by the witness himself.

In *re Nachman*, 8 A. B. R. 180, 184, 114 Fed. 995 (D. C. S. C.): "If he claims that the answer to any question propounded would tend to criminate him, he cannot be compelled to answer. This claim, to be effective, should be made by the witness himself, but the referee should notify him that a statement that such answer would tend to criminate him would, if false, subject him to a prosecution for perjury, as would any other false oath."

If testimony once be freely given or production of documents once be freely made, the testimony or documents may of course be used thereafter, for the privilege is purely personal and may be waived.

In *re Tracy & Co.*, 23 A. B. R. 438, 177 Fed. 532 (D. C. N. Y.): "Moreover, if freely given once, it may of course be used thereafter (*Tucker v. United States*, 151 U. S. 164), for the privilege is purely personal and may be waived. *Brown v. Walker*, 161 U. S. 591, 597."

In *re Bendheim*, 24 A. B. R. 254, 180 Fed. 918 (D. C. N. Y.): "Having volunteered upon a disclosure of what was in his shop at that time, he had waived his privilege, for it is well settled that having once embarked upon such a disclosure he has waived his privilege and cannot thereafter stop halfway."

^{94a}. See ante, § 1559; also compare impliedly, In *re Podolin*, 29 A. B. R. 406, 202 Fed. 1014 (D. C. Pa.); *Podolin v. Warner Dry Goods Co.*, 31 A. B. R. 796, 210 Fed. 97 (C. C. A. Pa. affirming, In *re Podolin*, supra).

⁹⁵. In *re Mellen*, 3 A. B. R. 226, 97

Fed. 326 (D. C. N. Y.); In *re Tracy & Co.*, 23 A. B. R. 438, 177 Fed. 532 (D. C. N. Y.).

⁹⁶. In *re Hark Bros.*, 14 A. B. R. 563, 564, 134 Fed. 109 (D. C. Penn.); In *re Tracy & Co.*, 23 A. B. R. 438, 177 Fed. 532 (D. C. N. Y.).

Even where the trustee has permitted such documents to be used by the state authorities in prosecution of the bankrupt in the state courts.⁹⁷

It has been held, however, that where the bankrupt or other witness has given the testimony or produced the document under coercion, as, for example, under the pressure of a court order, and not freely, the privilege would continue.^{97a}

Obiter, *In re Tracy & Co.*, 23 A. B. R. 438, 177 Fed. 532 (D. C. N. Y.): "Had the petitioner, for example, resisted the receiver and been compelled by an order of contempt to turn over his books, it might well be that he would retain the privilege. *Boyd v. United States*, 116 U. S. 616. I do not even say that the mere claim of privilege would not be enough to preserve his rights or that he was obliged to wait for the receiver actually to obtain an order of contempt against him."

§ 1562. Privilege Not Waived by Voluntary Bankruptcy.—The bankrupt does not waive the privilege by filing a voluntary petition.⁹⁸

U. S. v. Goldstein, 12 A. B. R. 760, 132 Fed. 789 (D. C. Va.): "It is suggested that one who files a voluntary petition in bankruptcy, who in theory, at least, knows that he may be required to make full disclosures under § 7, cl. 9, of the Bankruptcy Act is in the position of a defendant in a criminal case who voluntarily takes the witness stand in his own behalf, and that, having waived his constitutional privilege in respect to self-incrimination, he cannot refuse to answer any question. For the sake of argument it may be conceded—though I have not referred to, and have not found, any Virginia decision so holding—that, when a defendant in a criminal cause voluntarily goes on the stand and testifies in his own behalf, he cannot, on cross-examination, claim his privilege and

⁹⁷. *In re Tracy & Co.*, 23 A. B. R. 438, 177 Fed. 532 (D. C. N. Y.).

^{97a}. But compare, ante, § 1558; also *Johnson v. U. S.*, 227 U. S. 600, 30 A. B. R. 14, quoted at § 1558.

⁹⁸. *In re Hawthorn*, 2 A. B. R. 298 (Ref. La.). Contra, *In re Sapiro*, 1 A. B. R. 296, 92 Fed. 340 (D. C. Wis.): This case was rightly decided but was placed on the ground that the privilege was waived by voluntary bankruptcy rather than that the title of the documents itself had passed to the trustee by operation of law under § 70 (a) (1).

Also, compare, modification of contra rule, obiter, *In re Walsh*, 4 A. B. R. 693, 104 Fed. 518 (D. C. S. Dak.): "I will say, however, that it is not every question that the bankrupt may refuse to answer. He would not be protected in case a question was clearly cross-examination of what he had volunteered himself, either in his petition and schedules, or any testimony he had already given before the referee."

Compare, obiter, *quære*, *In re Hess*, 14 A. B. R. 562, 563, 134 Fed. 109 (D. C. Wash.).

Quære, if witness volunteers testimony tending to incriminate him does

he not waive the privilege on cross-examination as to same matters? *U. S. v. Goldstein*, 12 A. B. R. 760, 132 Fed. 789 (D. C. Va.); *In re Walsh*, 4 A. B. R. 693, 696, 104 Fed. 518 (D. C. S. Dak.).

Compare, *Com. v. Ensign*, 22 A. B. R. 797, 40 Pa. Super. Ct. 157.

Trustee Permitting Use of Documents or Testimony in State Prosecutions.—Although it is no part of the duty of the trustee, perhaps, to assist in the prosecution of a bankrupt in a State court for an offense connected with the assets or with the bankruptcy, yet it is not improper for him to do so and it may become, indeed, part of good citizenship for him to do so. *In re Tracy & Co.*, 23 A. B. R. 438, 177 Fed. 532 (D. C. N. Y.). Also, see ante, § 915.

Showing Books to Bankrupt's Business Rival.—If the trustee proceeds to show the books to trade rivals of the bankrupts so as to prejudice them in reestablishing themselves in business, it would clearly be wanton and illegal misuse of power. Obiter, *In re Tracy & Co.*, 23 A. B. R. 438, 177 Fed. 532 (D. C. N. Y.).

refuse to answer; and while there is some likeness between the two cases, the analogy is not perfect. It seems to me that the position of the bankrupt is rather more like that of a defendant in a criminal case, who has proposed to testify in his own behalf, and who before so doing concludes to claim his constitutional privilege."

§ 1562½. **Conditional Waiver of Privilege.**—It is possible that the witness may condition the production of the document or the giving of his testimony so as to limit its use, where the privilege otherwise would be absolute.

Obiter, *In re Tracy & Co.*, 23 A. B. R. 438, 177 Fed. 532 (D. C. N. Y.): "The delivery might have been conditional, but it was not. * * * So long as the petitioner retained his constitutional privilege, he might decline to assist any prosecution against himself; or he might surrender to this court his books only on condition, but when he waives it, he must waive it for all those purposes for which courts exist, and I cannot limit them so as to exclude the proposed use here."

§ 1563. **Pendency of Litigation with Witness, No Excuse for Refusing to Testify.**—The fact that a controversy, or even a law suit, is already pending in the state court with the witness, involving the same matter, and that the examination will oblige him to uncover his defense, will not excuse the witness from testifying. That is precisely what the examination is for—to ascertain the real facts pertaining to the bankrupt's acts, conduct and property;⁹⁹ nor is it a sufficient excuse that his answers will give evidence which the trustee may use in a subsequent civil action against him.¹ Disclosure of the truth cannot constitute an injury in the eyes of the law, except where it might tend to incriminate.

§ 1564. **Conversely, Pendency of Litigation Not Requisite.**—Conversely, an examination of a third person may be demanded although no action is pending and no issue joined.²

[1867] *In re Krueger*, 2 Low. 182: "These examinations thus stand in effect on the footing of summary bills of discovery. The discovery cannot be limited by reference to an action pending, for there is no such limitation in the law, but it is to be confined to the subject matter, the trade, dealings and estate of the bankrupt."

§ 1564½. **Right to Inspect Testimony Taken on General Examination.**—The testimony taken on general examination is part of the record in the case and is open to the inspection of all persons entitled to inspect such records.³

99. *In re Cliffe*, 3 A. B. R. 257, 97 Fed. 540 (D. C. Penn.).

1. *In re Howard*, 2 A. B. R. 584, 95 Fed. 415 (D. C. Calif., citing *In re Fay*, 3 N. B. Reg. 660; *In re Pioneer Paper Co.*, 7 N. B. Reg. 250; *Garrison v. Markley*, 7 N. B. Reg. 246).

2. *In re Fixen & Co.*, 2 A. B. R. 822, 96 Fed. 748 (D. C. Calif.); *In re Wilcox*, 6 A. B. R. 366, 109 Fed. 628 (C. A. N. Y.).

3. See ante, § 915; also, see *In re Samuelsohn*, 23 A. B. R. 528, 174 Fed. 911 (D. C. N. Y.), quoted at § 915.

Thus, a creditor who has not filed his claim is entitled to such inspection; ⁴ even though it will embarrass the trustee in bringing suit against such creditor later.⁵

§ 1565. Privileged Communications Respected.—Of course privileged communications are to be respected as much in bankruptcy as elsewhere. Thus, confidential communications between attorney and client are to be respected.

People's Bk. v. Brown, 7 A. B. R. 478, 112 Fed. 652 (C. C. A. N. J.): "This court has neither authority nor inclination to repudiate the rule which protects from exposure, unless with the client's consent, all communications between him and his counsel, made during the subsistence of that relation, in reference to any matter respecting which the latter has been, and properly could be, professionally consulted. This rule was applied, apparently for the first time, in the case of *Berd v. Lovelace*, Cary, '88, and for three centuries, at least, it has been steadily upheld by the courts upon the ground that for the proper administration of the law the confidence which it encourages the client to repose in the attorney to whom he resorts for legal advice and assistance should upon all occasions be inviolable. But it has been forcibly and vehemently assailed."

Thus, by statute, in Michigan the taxpayer's return to the assessors is privileged and may not be used for discovery of assets.⁶

But witnesses claiming the communication to be privileged may be subjected to preliminary examination to enable the court to determine for itself whether the communication sought for be, in the circumstances, a privileged one.

People's Bk. v. Brown, 7 A. B. R. 475, 112 Fed. 652 (C. C. A. N. J.): "Therefore, it is requisite that in every instance it shall be judicially determined whether the particular communication in question be really privileged, and, in order that such primary determination may be advisedly made, 't is indispensable that the court shall be apprised, through preliminary inquiry, of the characterizing circumstances. There is no presumption of privilege, and though its allowance may, in a clear case, be founded upon the voluntary statement of the attorney that his knowledge of the fact to which he is asked to testify was acquired in professional confidence, yet wherever, as in this case, the circumstances suggest that the sufficiency of the grounds of that statement should be considered, it is the right of the opposing party to demand that the proponent of the privilege shall be submitted to such interrogation as may be necessary to test its validity."

And the privilege does not extend to information gained by the attorney from other sources than confidential communications by his client.⁷ And a communication to a wife to be privileged must be confidential.⁸

§ 1566. Bankrupt's Wife Examined Touching "Business Relations."—But the bankrupt's wife may be required to submit to examination,

4. See ante, § 915; also, see *In re Samuelsohn*, 23 A. B. R. 528, 174 Fed. 911 (D. C. N. Y.), quoted at § 915.

5. See ante, § 915; also, see *In re Samuelsohn*, 23 A. B. R. 528, 174 Fed. 911 (D. C. N. Y.), quoted at § 915.

6. *In re Reid*, 17 A. B. R. 477 (D. C. Mich.).

7. *In re Ruos*, 20 A. B. R. 281, 159 Fed. 252 (D. C. Pa.).

8. *Jacobs v. United States*, 20 A. B. R. 550, 161 Fed. 694 (C. C. A. Mass.).

notwithstanding the general rule privileging transactions between husband and wife.⁹

This modification of the common law and statutory provision relative to privileged communications was a valuable amendment to the law, for before it was incorporated into the law it was possible to cover up the most frequently recurring kinds of fraud, namely, fraudulent transfers between husband and wife, both spouses hiding behind the privilege of the marital relation. To be sure, the amendment to § 21 (a) contains the proviso:

"Provided that the wife may be examined only touching business transacted by her or to which she is a party, and to determine the fact whether she has transacted or been a party to any business of the bankrupt."

But this proviso, on analysis, will be seen not to interfere greatly with a full and free investigation into all the business dealings between husband and wife.

Nevertheless the scope of the examination of the bankrupt's wife since the Amendment of 1903, is still not unlimited.

In *re Worrell*, 10 A. B. R. 744, 125 Fed. 159 (D. C. Pa.): "But, even in such an inquiry, she cannot be examined generally, the proviso to the clause specially confines the examination to 'business transacted by her, or to which she is a party, and to determine the fact whether she has transacted or been a party to any business of the bankrupt.' Her own separate business is, of course, not the subject of inquiry at all, but it is at this point precisely that questions are most likely to arise. Is the particular business her own, or is it her husband's? Obviously, she cannot be allowed to determine that question for herself, and the result is, that a certain degree of latitude in her examination must of necessity be permitted, in order that the court may be sure that she has not been, and is not now, transacting business as a mere cover for the bankrupt, or in aid of a scheme to injure his creditors. If the course of inquiry should reveal matters that, in the end, turn out to concern herself alone, such a result is to be regretted; but this cannot always be obviated, and it is certainly better than to allow her to decide conclusively that the business is hers by making a bare assertion to that effect."

§ 1567. Competency of Witnesses Governed by What Law.—The competency of witnesses in bankruptcy is, to be sure, governed by the Federal law, Rev. Stat., U. S.; § 858, together with such modification as the Amendment of 1903, § 21 (a) introduces, by making a wife competent touching business transactions with her husband.¹⁰

9. Bankr. Act, § 21 (a), as amended. Compare, as to rule before the Amendment of 1903, In *re Mayer*, 3 A. B. R. 222, 96 Fed. 826 (D. C. Wis.); In *re Cohn*, 5 A. B. R. 16, 104 Fed. 328 (D. C. Mo.); In *re Jefferson*, 3 A. B. R. 174, 96 Fed. 826 (D. C. Wash.); In *re Fowler*, 1 A. B. R. 555, 93 Fed. 417 (D. C. Wis.).

10. Bankr. Act, § 21 (a): "A court of bankruptcy may, * * * require any designated person, including the

bankrupt and his wife, to appear * * * to be examined concerning the acts, conduct or property of a bankrupt whose estate is in process of administration under this Act: Provided, That the wife may be examined only touching business transacted by her or to which she is a party, and to determine the fact whether she has transacted or been a party to any business of the bankrupt."

Smith v. Township, 17 A. B. R. 748, 150 Fed. 257 (C. C. A. Mich.): "It was objected to the testimony of Chamberlain above recited that he was an incompetent witness in regard to the transactions between himself as agent of the bonding company and the bankrupt, because of a statute of Michigan excluding the testimony of one who has acted as an agent for one party to a transaction, where the other party has since deceased, relative to any matter equally within the knowledge of such other party. This objection is renewed here. But this proceeding was in a federal court, and as the statute of the United States relating to the competency of witnesses, as affected by their interests, covers the subject and is paramount, the State statute is not the test, as the District Judge rightly held."

But Revised Statutes of the United States, § 858, was amended by the Act of June 27, 1906, under which it has been held that the law of the state wherein the Federal court is held is to govern as to the competency of witnesses.¹¹ But, of course, this amendment of Revised Statutes, § 858, does not prevail over the specific provision of § 21a, of the Bankruptcy Act, making the wife a competent witness in bankruptcy proceedings. So, since the Amendment of June 27, 1906, to Revised Statutes, § 858, and the Amendment of 1903 to the Bankruptcy Act, § 21a, the complete statement of the competency of witnesses in the bankruptcy courts is as follows: The competency of witnesses to testify in bankruptcy is governed by the state law wherein the particular federal court is sitting, except that, regardless of state law, a party may not testify to transactions with a deceased person where the opposite party is the executor or administrator, and also except that the wife of the bankrupt may be examined, but be examined only, touching business transacted by her with or for the bankrupt or to which she is a party and to determine the fact whether she has transacted or been a party to any business of the bankrupt.

§ 1568. Contempt for "Willfully Evasive" or "Flagrantly False" Testimony.—The bankruptcy court has power to punish a witness for contempt for willfully evasive or flagrantly false testimony on general examination.¹² And such false swearing is punishable as a contempt although also punishable as a crime.¹³

In *re Fellerman*, 17 A. B. R. 785, 149 Fed. 244 (D. C. N. Y.): "Perjury in the presence of the court is a contempt as old as the courts themselves. It is 'undoubtedly a great contempt.' *Stockham v. French*, 1 Bing. 365."

11. In *re Hoffman*, 28 A. B. R. 680, 199 Fed. 448 (D. C. N. Y.); In *re Thompson*, 28 A. B. R. 794, 197 Fed. 681 (D. C. N. Y.); [before amendment of June 27, 1906] In *re Josephson*, 9 A. B. R. 349 (D. C. Ga.). Also, see § 551.

12. In *re Fellerman*, 17 A. B. R. 785, 149 Fed. 244 (D. C. N. Y.); In *re Michaels*, 28 A. B. R. 38. See post, § 2331; also, obiter, In *re Gitkin*, 21 A. B. R. 113, 164 Fed. 71 (D. C. N. Y.), quoted at § 2331; *Ex parte Bick*, 19 A.

B. R. 68, 155 Fed. 908 (D. C. N. Y.), quoted at § 2331; In *re Schulman*, 21 A. B. R. 288, 164 Fed. 440, 167 Fed. 231 (D. C. N. Y.), quoted at § 2331; In *re Cashman*, 21 A. B. R. 285, 168 Fed. 1008 (D. C. N. Y.), wherein the defense of insanity was raised but found not sustained by the proof; In *re Schulman*, 23 A. B. R. 809, 177 Fed. 191 (C. C. A. N. Y.), affirming 21 A. B. R. 288, quoted at § 2331.

13. Obiter, In *re Gitkin*, 21 A. B. R. 113, 164 Fed. 71 (D. C. Pa.).

"It is a 'gross piece of contempt.' Chicago Directory Co. v. U. S. Directory Co., 123 Fed. 194."

Thus, repetitions of "I don't know" or "I don't remember," about matters which undoubtedly must have been known by the witness and must have been in his memory, may be contempt.¹⁴

§ 1568½. Attendance of Bankrupts or Witnesses Confined as Prisoners or in Institutions.—The attendance of bankrupts or witnesses confined as prisoners or in asylums may be procured by the writ of habeas corpus ad testificandum. This writ is not the high prerogative writ of habeas corpus, but is merely the ancient common-law precept, now authorized by statute, to bring a prisoner into court to testify; and it may be granted and issued by the court at chambers; but its issuance is a matter of discretion, even in cases where the prisoner is the bankrupt and his testimony is wanted at the first meeting of his creditors.

In re Thaw, 21 A. B. R. 561, 166 Fed. 71 (C. C. A. Pa., affirming S. C., 22 A. B. R. 687, 172 Fed. 288): "That the writ under consideration was rightfully allowed in the first instance need not be questioned, and we think is not questionable; but in our opinion it is likewise clear that the order under which it was issued was subject to revocation and the writ itself to annulment. * * * That writ was not the high prerogative writ of habeas corpus, the great object of which is deliverance from unlawful imprisonment, and which either a court, a justice, or a judge may grant and adjudicate, but was merely the ancient common-law precept to bring a prisoner into court to testify, and it was none the less the process of the court from which it issued because the order for its issuance emanated from a judge at chambers. It was granted and issued to bring a prisoner before the United States District Court at Pittsburg, in order that his testimony might there be taken, and it was directed to the custodian of his person, not that an 'inquiry into the cause of restraint of liberty' might be made, but with an object analogous to that sought to be attained by directing a subpœna duces tecum to the custodian of an evidential document, who, of course, upon cause shown, may subsequently be excused from producing it. 'If the desired witness is confined in jail [or in a State hospital for the criminal insane] a subpœna would be of no avail, since he could not obey it and his custodian would still lack authority to bring him. Accordingly a writ to the custodian is necessary, ordering the prisoner to be brought to give testimony. This writ of habeas corpus ad testificandum, grantable in discretion at common law, is now usually authorized by statute as a matter of course.' Wigmore on Evidence, vol. 4, § 2199. It is unnecessary, we think, to say anything further in support of our conclusion that the District Court, 'Judge James S. Young presiding,' did not overstep its lawful authority in quashing the writ in question, unless, as has been suggested, the scope of its general power in this respect was in some way curtailed by § 7 of the Bankruptcy Act. * * * That section, no doubt, makes it the duty of a bankrupt to attend the first meeting of creditors, and to do

14. See post, § 2331; In re Cashman, 21 A. B. R. 285, 168 Fed. 1008 (D. C. N. Y.); In re Schulman, 21 A. B. R. 288, 164 Fed. 440, 167 Fed. 231 (D. C. N. Y.), quoted at § 2331; In re Gitkin, 21 A. B. R. 113, 164 Fed. 71

(D. C. N. Y.), quoted at § 2331; In re Bick, 19 A. B. R. 68, 155 Fed. 908 (D. C. N. Y.), quoted at § 2331; In re Schulman, 23 A. B. R. 809, 177 Fed. 191 (C. C. A. N. Y.), quoted at § 2331. See post, § 1861.

the several other things there enumerated; but it does not follow, as seems to be supposed, that a 'writ of habeas corpus ad testificandum * * * to produce the bankrupt for examination * * * is a right which his creditors have, and * * * which the bankrupt also has,' and that therefore it must be allowed, upheld, and enforced, regardless of circumstances and conditions. The rule of the common law has always been that this writ, which for centuries has been used to bring prisoners into court to testify, is 'grantable in discretion,' and we have not been convinced that by forced implication there should be attributed to Congress the unexpressed intent to abrogate that rule, and to take from the courts of bankruptcy their wholesome supervisory control of a process which manifestly is capable of misemployment, perversion and abuse. We accordingly hold that the question raised by the petition to quash was for determination in the exercise of a sound judicial discretion."

And it may be refused where the bankrupt may be examined at the place of his confinement.¹⁵

§ 1569. Attendance of Witnesses Residing Out of State or Farther than One Hundred Miles.—It has been held that a witness cannot be compelled to appear for examination before a referee at a place more than one hundred miles distant from his residence, even if it be within the state; and that if his testimony is sought, it can be required only under the rule of the succeeding sections;¹⁶ also that a witness may not be compelled in bankruptcy proceedings to appear for examination before a referee at a place outside the state of the witness' own residence.¹⁷ But these cases seem not only wrong on reason but also to be founded on a misconstruction of the proviso of § 41 of the Act. Indeed, it is necessary to change the word "and" to "or" in that section of the Act in order to arrive at the conclusion reached in the cases criticised. The proviso of § 41 manifestly refers merely to the established rule that a witness may be subpoenaed from without the state if within one hundred miles of his residence, Congress evidently merely seeking to make it clear that nothing in the Act should be held to authorize the calling of a witness from without the state, if resident at a greater distance than one hundred miles from the place of hearing.

§ 1570. General Examination of Non-Resident Bankrupt or Witness before Another Referee, or State Judge.—The bankrupt or any other witness may be ordered by ancillary proceedings to appear in another district before another referee or the judge of any state court to submit to examination there.¹⁸

And habeas corpus ad testificandum may be refused to bring the bankrupt from another State where he is being confined in an asylum for the

15. See post, § 1570.

16. In re Hemstreet, 8 A. B. R. 760, 117 Fed. 568 (D. C. Iowa).

17. In re Cole, 13 A. B. R. 300, 133 Fed. 414 (D. C. Me.); (1867) Paine v. Caldwell, Fed. Cas. 10,674; In re Hem-

street, 8 A. B. R. 760, 117 Fed. 568 (D. C. Iowa).

18. Obiter, In re Robinson, 24 A. B. R. 617, 179 Fed. 724 (D. C. Minn.); impliedly, Babbitt v. Dutcher, 23 A. B. R. 519, 216 U. S. 102.

criminal insane, if he can be examined at the place of his confinement.¹⁹

§ 1571. **Order for Examination in Another District, Whether Ancillary Proceedings Requisite.**—A serious question arises where it is desired to take the examination of the bankrupt or of a witness in another district. Before the case of *Babbitt v. Dutcher* [216 U. S. 102] upholding the ancillary jurisdiction of the bankruptcy courts, it had been held by some of the courts which had denied such jurisdiction that the requisite "order" for the general examination, under Bankr. Act, § 21 (a), was to be issued in the original bankruptcy proceedings though served upon the witness in the other district for his appearance before a referee or state judge therein;²⁰ but it is exceedingly doubtful that the court has jurisdiction to issue an order for service out of its own district, even a mere order for examination,²¹ for the power of the bankruptcy courts is confined to their respective territorial limits,²² and there would be no power, furthermore, to punish for disobedience of such order²³ committed in such other district.²⁴ At any rate, such examination may be had in ancillary proceedings.²⁵

Obiter, In re Robinson, 24 A. B. R. 617, 179 Fed. 724 (D. C. Minn.): "It is thus seen that, if the petitioners have the right to an examination of McMasters under § 21a of the Bankruptcy Act, they can obtain it by application to the United States District Court for the Southern District of Illinois. Under these circumstances, I do not feel called upon to decide whether under that section this court has any authority to issue an order requiring McMasters to appear before the referee in bankruptcy at Rock Island, or whether it can authorize the referee himself to require such appearance. Even if this court did have that power, there are certain practical objections in the way of issuance of a subpoena, punishment for contempt, and other matters which might be referred to, that justify me in requiring the petitioners to proceed before the Illinois court. It seems to me, however, that the case does not fall under paragraph 'a,' § 21, but rather under paragraph 'b' of the same section, which is as follows: 'The right to take depositions in proceedings under this Act shall be determined and enjoyed according to the United States laws now in force, or such as may be hereafter enacted relating to the taking of depositions, except as herein provided.'"

Ancillary proceedings can only be instituted "in aid of" a receiver or trustee, and presumably must be instituted by him or in his name; so that the bankrupt or a creditor, as such, may not, in his own name, obtain such

19. In re Thaw, 22 A. B. R. 687, 172 Fed. 288 (D. C. Pa., affirming 21 A. B. R. 561, C. C. A.), quoted at § 1568½; compare, ante, § 1568½.

20. In re Williams, 10 A. B. R. 541, 123 Fed. 321 (D. C. Tenn.). Compare, In re Geo. Watkinson Co., 12 A. B. R. 370, 130 Fed. 218 (D. C. Pa.); also compare, In re Sturgeon, 14 A. B. R. 681, 138 Fed. 608 (C. C. A. N. Y.).

21. In re Sutter Bros., 11 A. B. R. 632, 131 Fed. 654 (D. C. N. Y.); In re Robinson, 24 A. B. R. 617, 179 Fed. 724 (D. C. Minn.).

22. Bankr. Act, § 2, "* * * are hereby invested, within their respective territorial limits * * * etc."

23. In re Robinson, 24 A. B. R. 617, 179 Fed. 724 (D. C. Minn.).

24. *Obiter* and inferentially, In re Robinson, 24 A. B. R. 617, 179 Fed. 724 (D. C. Minn.).

25. Impliedly, *Babbitt v. Dutcher*, 216 U. S. 102, 23 A. B. R. 519; In re Madson Steel Co., 216 U. S. 115, 23 A. B. R. 614; [1867] In re Tift, 19 Nat. Bankr. Reg. 201.

an examination in another district but may only do so when authorized by the bankruptcy court to use the receiver's or trustee's name, notwithstanding the unqualified words of § 21 (a) granting such examination on the application of "any officer, bankrupt or creditor * * *." On theory, however, it is to be remembered that the exercise of the drastic power of examination into the "acts, conduct and property of a bankrupt," peculiar to bankruptcy law, is justified only on the basis that it is requisite in order to aid the receiver or trustee in the administration of the estate; and that it is not to be considered to be given as an independent right to be exercised by creditors or by the bankrupt in their individual interests. It is furthermore to be presumed that the bankruptcy court would be prompt to permit a creditor or the bankrupt to use the receiver's or trustee's name for such examination, where satisfied that it might aid in the proper administration of the estate, whether the receiver or trustee thought differently or not.

§ 1572. Method Where before Judge of State Court or Another Referee.—But where the witness thus appears for examination at a place other than that where the proceedings themselves are pending, the referee, or judge, acting in the examination, perhaps should take down all the testimony, merely noting the objections and not ruling upon them, such examination to be thereupon filed with the referee in charge of the proceedings proper, who may himself then pass upon the admissibility of the testimony.²⁶

§ 1572½. Depositions.—The right to take depositions in proceedings in the bankruptcy courts is in general determined and exercised according to the rules of the federal courts.²⁷ However, notice of the taking of such deposition is to be filed with the referee in each case;²⁸ such rule being based probably on the double ground of enabling all parties interested to keep themselves informed, if they wish, as to the progress of the administration and also perhaps of supplying a sort of service of notice upon the whole body of creditors. When depositions are to be taken in opposition to the allowance of a claim, notice must be served upon the claimant, and when in opposition to a discharge notice also must be served upon the bankrupt.²⁹

26. *In re Sturgeon*, 14 A. B. R. 681, 138 Fed. 608 (C. C. A. N. Y.). But compare, ante, § 1554. The distinction made by the able judge in *In re Wilde's Sons*, 11 A. B. R. 714, 131 Fed. 142 (D. C. N. Y.), cited supra, however, ought to be noted, as laying down the better rule.

27. Bankr. Act, § 21 (b): "The right to take depositions in proceedings under this act shall be determined and enjoyed according to the United States laws now in force, or

such as may be hereafter enacted relating to the taking of depositions except as herein provided."

Whether deposition suppressed for refusal to answer cross interrogatories because tending to incriminate. Compare, *Carey v. Donohue*, 31 A. B. R. 210, 209 Fed. 328 (C. C. A. Ohio).

28. Bankr. Act, § 21 (c): "Notice of the taking of depositions shall be filed with the referee in every case. * * *"

29. Bankr. Act, § 21 (c): "* * * When depositions are to be taken in

Probably a general examination into the "acts, conduct and property" of the bankrupt can only be had upon order duly made in accordance with § 21 (a) and not by way of deposition under § 21 (b). But a deposition under § 21 (b) rather than an examination under § 21 (a) is the appropriate method in opposition to discharge, for, as we have seen [ante, § 1555], the general examination is not to be considered as a general deposition admissible in any and all controversies whatsoever that might arise in the course of the proceedings but is a mere general discovery, admissible in subsequent litigation only by stipulation of counsel or as an admission against interest in some controversy with the very witness himself as a party litigant.³⁰

§ 1573. Witness, as Such, Not Entitled to Attorney.—A witness is not entitled as such to have an attorney, and his attorney need not be allowed to participate in the proceedings.³¹

In *re Abbey Press*, 13 A. B. R. 11, 134 Fed. 51 (C. C. A. N. Y.): "Finally, it is contended that the petitioner was entitled to be represented by counsel.

"No authority is cited in support of this proposition. Such a course would be contrary to the rulings in other courts, and, as we understand it, contrary to the practice and decisions in the bankruptcy courts. In any event, no such representation should be allowed except in the discretion of the court, that is, of the referee."

§ 1574. But Is Entitled if Witness Be Creditor or Bankrupt.—But if the witness is also a creditor who has proved his claim in the proceedings, or if he is the bankrupt himself,³² it would seem he may, as being a party to the proceedings, be entitled to an attorney and to have his attorney heard on the propriety of questions and to participate in the examination precisely as could any creditor who is not a witness. A contrary rule would allow creditors who were not witnesses to have attorneys participate in the examination, but would debar creditors who were witnesses from the exercise of the same right. So, also, by the same contrary rule, a bankrupt, who in fact is precisely as much of a party to the proceedings as any creditor, would not be entitled to have his attorney participate in the examination when the bankrupt himself was a witness, but would be entitled to participate in the proceedings when he was not a witness. The contrary rule thus would lead to absurdity.

So, while it still remains true that as a mere witness neither a bankrupt

opposition to the allowance of a claim, notice shall also be served upon the claimant, and when in opposition to a discharge notice shall also be served upon the bankrupt."

30. In *re Robinson*, 24 A. B. R. 617, 179 Fed. 724 (D. C. Minn.), quoted at § 1572.

31. See In *re Howard*, 2 A. B. R. 582, 95 Fed. 415 (D. C. Calif.), citing In *re Comstock*, 13 N. B. Reg. 193, Fed.

Cases, No. 3,080, and In *re Fredenburg*, 1 N. B. Reg. 268, Fed. Cases, No. 5,075, and In *re Stuyvesants' Bk.*, 6 Ben. 33, Fed. Cases, No. 13,582. In *re Cobb*, 7 A. B. R. 104 (Ref. Mass., affirmed by D. C. without report). But see In *re Fixen*, 2 A. B. R. 822, 96 Fed. 748 (D. C. Calif.).

32. Contra, In *re Adler & Co.*, 21 A. B. R. 302.

nor any creditor is entitled to counsel, yet, as parties to the bankruptcy proceedings they are so entitled, and both the bankrupt's attorney, and also any creditor's attorney, is entitled to cross-examine witnesses, where the examination is a "general" examination.³³

In *re Hark Bros.*, 14 A. B. R. 624, 136 Fed. 986 (D. C. Pa.): "It is to be assumed that the referee will allow a bankrupt representation by counsel at any hearings that may take place."

§ 1575. Witness' Fees and Mileage.—Witnesses, except the bankrupt, are entitled to \$1.50 for each day's attendance, and 5 cents per mile for each mile going and 5 cents for each mile returning.³⁴ The wife or husband of the bankrupt is entitled to the fee, the same as any other "designated person."³⁵ The fees and mileage must be tendered to the witness at the time of service,³⁶ else contempt for disobedience of the subpœna will not lie.

§ 1576. Contempt for Disobedience of Subpœna.—Witnesses may be punished for contempt for failure to respond to a subpœna to attend before a referee. But where the witness is required to attend more than one hundred miles from his residence, he should not be attached for contempt for failure to respond unless he has been tendered his fee and mileage.³⁷

§ 1577. No Witness Fees to Bankrupt, but Expenses, Where Examined Away from His Town.—A bankrupt is not entitled to any fees or compensation for attending the court for examination, except that "he shall be paid his actual expenses from the estate when examined or required to attend at any place other than the city, town or village of his residence;"³⁸ although this provision for reimbursement would not extend to his attendance upon the hearings upon his application for discharge.³⁹

33. *Contra*, In *re Cobb*, 7 A. B. R. 104 (Ref. Mass., affirmed by D. C.). *Contra*, In *re Adler & Co.*, 21 A. B. R. 302 (D. C. La.).

34. Section 848, U. S. Rev. Stat.

Claimant re-examined upon reconsideration of his claim has been held entitled to reimbursement for his reasonable traveling expenses and hotel bills but not counsel fees, where an agreement to that effect has been made, In *re Geo. Watkinson Co.*, 12 A. B. R. 370, 130 Fed. 218 (D. C. Penn.). Otherwise such reimbursement would be clearly improper.

35. In *re Marcus*, 20 A. B. R. 397, 160 Fed. 229 (D. C. Vt.).

36. In *re Boeshore*, 10 A. B. R. 802 (D. C. Penn.); In *re Kerber*, 10 A. B. R. 747, 125 Fed. 653 (D. C. Penn.).

37. In *re Kerber*, 10 A. B. R. 747,

125 Fed. 653 (D. C. Penn.); In *re Boeshore*, 10 A. B. R. 802 (D. C. Penn.).

Mere Order, While Witness on Stand, to Bring Document Held, under Facts of Case, Not Sufficient, in Absence of Notice or of Subpœna Duces Tecum, and Failure to Bring Not Contempt.—A mere order on a witness while he is on the stand, to bring in a document at a later hearing, has been held under the circumstances not sufficient, over his protest and in the absence of notice or of a subpœna duces tecum, and failure to produce it has been held not contempt. In *re Johnson & Knox Lumber Co.*, 18 A. B. R. 51, 151 Fed. 207 (C. C. A. Ills.).

38. Bankr. Act, § 7 (9).

39. *Obiter* and *inferentially*. In *re Shanker*, 15 A. B. R. 109, 138 Fed. 862 (D. C. Penn.).

§ 1578. Bankrupt Voluntarily Removing Residence after Adjudication Not Entitled to Reimbursement.—If the bankrupt voluntarily remove his residence, after he has been adjudicated bankrupt, he would not be entitled to such reimbursement and could not saddle the extra expense upon his creditors.

In re Groves, 6 A. B. R. 732 (Ref. Ohio affirmed by D. C.): "The bankrupt is not entitled to reimbursement for his expenses in returning for examination, where he has voluntarily removed his residence from the district after bankruptcy."

§ 1579. Employment of Stenographer.—Upon the application of the trustee an order may be made by the referee authorizing him to employ a stenographer at the expense of the estate to take down the general examination of the bankrupt and witnesses and for other examinations, but the statute itself prescribes that the estate shall not be liable for the expense of such employment beyond the rate of ten cents per folio, that is to say, per 100 words, for both taking down and transcribing the testimony.⁴⁰

In re Ellett Elec. Co., 28 A. B. R. 453, 196 Fed. 400 (D. C. N. Y.): "As to the allowances. According to the certificate of the referee, the assets of the bankrupt estate realized \$590.78, and he made allowances to the trustee, his attorney, to the attorney of the bankrupt, and to stenographers amounting to \$325.94, leaving a balance of \$164.84, taking into consideration the disapproval of the Ellett claim, for distribution among preferred creditors. In view of the services rendered, certain of the allowances are thought excessive.

"The record consists of 53 pages, of which only about 30 are testimony. The stenographers were allowed \$62.12, which amount is inordinate. Where three duplicate copies are supplied, a charge of 40 cents per page has in other cases that have come before this court been held a fair and reasonable compensation. The assets of the estate were known to the trustee at the time the Ellett claim against the bankrupt was before the referee to be insufficient to pay in full the preferred claims; therefore, it would have been sufficient to have taken the substance of the evidence arising on the disputed claim, and a summary disposition would have been proper. If the claimant desired a fuller examination or more complete record, he himself should have borne the stenographer's expenses. By § 38, subd. 5, of the Bankruptcy Act, on the application of the trustee, a stenographer may be employed at the expense of the estate, but the compensation cannot exceed 10 cents per folio for reports and transcripts of the proceedings. In view of the fact that three duplicate copies were furnished, perhaps a reasonable additional compensation would not have been subject to criticism, though I think that additional copies should be paid for by the parties desiring them. The large outlay for stenographer's fees and charges before referees and special masters in bankruptcy is a serious barrier to an economical administration of estates in bankruptcy, and such expenses should be curtailed whenever possible. In the federal courts, where there is no official stenographer, the expense for taking shorthand notes of examination and transcribing the

40. Bankr. Act, § 38 (5): "Referees may 'upon application of the trustee during the examination of the bankrupt or other proceedings authorize the employment of stenographers at the

expense of the estate at a compensation not to exceed 10 cents per folio for reporting and transcribing the proceedings." In re Todd, 6 A. B. R. 88, 109 Fed. 265 (D. C. N. Y.).

same is usually divided by the litigants and taxed to the extent of the amount paid in favor of the prevailing party. The record in this case does not show that the trustee authorized the employment of the stenographers or objected thereto. As much of the expenses was incurred in conducting the examination relating to the Ellett claim, the expense for stenographer's services should rightly fall on the defeated party, but, as no objection to the employment of a stenographer was made by the trustee, I will allow an expense not exceeding \$21.20, or 40 cents per page for the three copies of testimony to be charged against the estate."

The statutory provision, of course, does not mean that the stenographer is compelled to work at such rate of compensation, but only that such part of the compensation as will be at the rate of ten cents per folio shall be charged against and paid for from the estate. Evasions of this provision of the law are not to be tolerated. Creditors may personally make up any deficiency if the stenographer is unwilling to take the compensation which may be charged against the estate. And if the testimony be not transcribed, the provisions of § 38 (5) would not forbid the allowance of a per diem to the stenographer, for taking down the testimony in shorthand.

However, the strict wording of the statute, § 38 (5), mentions only the trustee as the applicant for leave to employ a stenographer at the expense of the estate, and it has been held that the trustee must make the application.⁴¹ It has also been held that different rules are to prevail before the adjudication and reference to the referee.⁴²

Where there are no funds in the estate, if the bankrupt desires the testimony on general examination to be taken down in writing, he may be compelled to furnish indemnity therefor.⁴³

41. In re Todd, 6 A. B. R. 88, 109 Fed. 265 (D. C. N. Y.).

Fed. 694 (D. C. N. Y.). But compare, § 1543.

42. In re Stark, 18 A. B. R. 467, 155

43. In re Goldstein, 19 A. B. R. 96, 155 Fed. 695 (D. C. N. Y.).

CHAPTER XXXII.

JURISDICTION OF THE BANKRUPTCY COURT WHERE ANOTHER COURT ALREADY HAS CUSTODY: CONFLICT OF JURISDICTION.

Synopsis of Chapter.

- § 1580. Jurisdiction and Conflict of Jurisdiction in Collecting and Protecting Assets.
- § 1581. Courts Cautious in Dealing with Conflict of Jurisdiction.
- § 1582. If State Court First Obtains Possession, It Retains Jurisdiction, Except in Three Instances.
- § 1583. Simply because Bankruptcy Court Preferable or Trustee Interested, Not Sufficient to Confer Jurisdiction.
- § 1584. But State Courts May Be Permitted to Retain Jurisdiction Where Better Suited to Adjust Rights, Even Where Bankruptcy Court Might Have Jurisdiction.
- § 1584½. Or Bankruptcy Court May Surrender Custody.
- § 1585. Replevin and Other Suits Asserting Ownership, Where Seizure Made First by State Court, Not Abated.
- § 1586. Foreclosure and Other Suits Not Themselves Creating Liens Nullified by Bankruptcy, but Simply Enforcing Liens, etc., Not Abated, Where Started before Bankruptcy.
- § 1587. Custody of State Court Preserved in Part, and in Part Superseded.
- § 1588. Attachments Obtained Prior to Four Months, Not Abated.
- § 1589. Landlord's Levy.
- § 1590. Partnership Dissolution Suits.
- § 1591. Fraudulent Transfer Suits Instituted before Four Months.
- § 1592. Fraudulent Transfer Suit within Four Months in Aid of Levy Made before Four Months, Not Abated.
- § 1593. Creditors' Bills Instituted before Four Months.
- § 1594. Assignments and Receiverships Created before Four Months.
- § 1595. Administrators, etc., Where Bankrupt Owns Interest in Estate, Not Disturbed.
- § 1595½. Awards of Arbitrators.
- § 1596. Trustee's Intervention in State Court Proceedings Does Not Oust State Court.
- § 1597. State Courts Administer Bankrupt Law and Trustee, Intervening, Not Confined to Rights Accorded by State Law.
- § 1598. Bankruptcy Court May Enjoin to Permit Intervening of Trustee.

DIVISION 1.

- § 1599. First Exception to Rule That State Court Retains Jurisdiction if First Obtaining Possession.
- § 1600. Same Subject Discussed, Ante, "Liens by Legal Proceedings Nullified by Bankruptcy."
- § 1601. When Lien Nullified Property Recoverable by Summary Order.

DIVISION 2.

- § 1602. Second Exception to Rule That State Court Retains Jurisdiction if First Obtaining Custody.

- § 1603. Basis of Superseding Custody of Assignee and Receiver.
- § 1604. Possession under General Assignments Superseded.
- § 1605. Likewise, under State Court Receiverships.
- § 1606. General Assignment Not Per Se Illegal nor Void but Voidable Merely.
- § 1607. Unless Petition Filed within Four Months, Followed by Adjudication, State Court's Custody Not Superseded.
- § 1608. But if Filed within Four Months and Adjudication Occurs, Assignment Void.
- § 1609. Until Adjudication, Custody Not Superseded.
- § 1610. Assignee or Receiver May Be Enjoined.
- § 1611. May Be Ordered Summarily to Surrender Assets.
- § 1611½. But Only on Due Notice and Hearing.
- § 1612. No Summary Order as to Sums Already Disbursed.
- § 1613. Sales by Assignee under Void Assignment.
- § 1614. Assignee Has Lien upon Surrendered Assets for Expenses and Compensation.
- § 1615. Assignment Must Be "General" and "Bona Fide," Not "Partial" nor "Fraudulent."
- § 1616. Receivers Likewise Entitled to Lien Where Receiverships Nullified by Bankruptcy.
- § 1617. Likewise, Mortgagees in Possession under Mortgage Executed for Benefit of All Creditors Assenting.
- § 1617½. Transferees under Arrangements for Effecting Compositions Out of Court.
- § 1618. Also, Attaching Creditors Where Attachment Lien Preserved for Benefit of Estate.
- § 1619. Where Attachment Really for Benefit of All, Creditor Entitled to Reimbursement.
- § 1620. Whether Extent of Lien May Be Fixed by State Court before Surrender.
- § 1621. Only Expenses and Compensation for Services Beneficial to Estate and Reasonable, Allowed.
- § 1622. Others' Rights, to Be Worked Out Through Assignee or Receiver.
- § 1623. How Assignee's or Receiver's Rights to Be Presented.
- § 1623½. Adverse Claimant's Rights Preserved.
- § 1624. Liability on Assignee's Bond on Superseding of State Court's Custody.

DIVISION 3.

- § 1625. Third Exception to Rule That State Court Retains Jurisdiction if First to Obtain Custody.
- § 1626. Basis of Supersedence, Paramount Authority Conferred by Constitution, and Necessary Implication from § 70.
- § 1627. State Bankruptcy and Insolvency Laws Not Prohibited.
- § 1628. But Suspended during Existence of Federal Bankruptcy Law, as to All Classes Subjected to Latter.
- § 1629. State Insolvency and Bankruptcy Laws Ipso Facto Suspended.
- § 1630. Not Suspended nor Inopèrative as to Classes Not Covered by Federal Bankruptcy Act.
- § 1631. State Bankruptcy and Insolvency Laws Simply Held in Abeyance.
- § 1632. Bankruptcy and Insolvency Laws, and General Assignment Laws, Distinguished.
- § 1633. Various Holdings as to What Amount to "Insolvency" Proceedings.

- § 1634. Receiverships and Winding Up of Insolvent Corporations, Whether Insolvency Proceedings.
- § 1635. Procedure to Procure Surrender from State Bankruptcy or Insolvency Courts.
- § 1636. Thus, State Court Receiver May Be Enjoined.
- § 1637. Comity Requires Resort First to State Tribunal.

DIVISION 4.

- § 1638. Voluntary Surrender by State Court.

SUBDIVISION "A."

- § 1639. Pending Suits against Bankrupt—Subrogation of Trustee to Creditor's Lien Where Lien Preserved.
- § 1640. Pending Suits by Bankrupt—Substitution of Trustee.
- § 1641. Preliminary Order of Approval Proper.
- § 1642. Probability of Success Should Appear.
- § 1643. Only Suits on Rights Passing to Trustee Authorized.
- § 1644. Defendant Not Released by Failure of Trustee to Assume Prosecution.
- § 1645. Ordering Trustee to Apply for Leave to Defend.
- § 1646. Intervening Not Usually Proper Except Where Property Involved.
- § 1647. Intervening in Suits in Personam.
- § 1648. State Court Governed by State Law and Judicial Policy in Granting or Refusing Application.
- § 1649. Manner of Intervention.
- § 1650. Trustee Bound as Any Other Litigant, on Intervention.
- § 1650½. Making Trustee Party Defendant.
- § 1651. Stay of Pending Suits.

§ 1580. Jurisdiction and Conflict of Jurisdiction in Collecting and Protecting Assets.—In the orderly development of the treatise, the subject is now reached of the forum for the assertion of rights in collecting assets belonging to the estate and in defending possession of them when custody is once acquired. The sections of the Bankruptcy Act involved are §§ 2 (7), 23, 38, 60 (b), 67 (e) and 70 (e).¹

§ 1581. Courts Cautious in Dealing with Conflict of Jurisdiction.—Courts must be cautious in dealing with a conflict of jurisdiction.²

But at the proper time the federal courts may by force emphasize the supremacy of the constitution:

Hooks v. Aldridge, 16 A. B. R. 665, 145 Fed. 865 (C. C. A. Tex.): "While it is unquestionable that the federal courts are the final arbiters to settle questions arising under the bankruptcy laws, there are questions relating to comity and procedure, in the event of conflict of opinion between the State courts and the bankruptcy courts as to the possession of the bankrupt's assets, which remain unsettled by decision of the Supreme Court. Whether the bankruptcy courts should make such orders as will preserve the estate, and await the final result of the litigation—

1. In re MacDougall, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.).

2. Metcalf v. Barker, 9 A. B. R. 46, 187 U. S. 175; Pickens v. Dent, 5 A. B. R. 644 (C. C. A. W. Va., affirmed in

187 U. S. 175, but this point not adverted to); *Hooks v. Aldridge*, 16 A. B. R. 664, 145 Fed. 865 (C. C. A. Tex.). Impliedly, In re Dana, 21 A. B. R. 684, 167 Fed. 529 (C. C. A.).

tion in the State court, or should act on its own opinion of the want of jurisdiction of the State court, and enforce its order to secure the possession of the property, is one of the questions left unsettled, so far as we are advised, by a decision of the Supreme Court. At a proper time the federal courts, of course, may decree the enforcement of the supremacy of the Constitution and laws of the United States, for it is an "incontrovertible principle that the government of the United States may, by means of physical force, exercised through its official agents, execute on every foot of American soil the powers and functions that belong to it."

And the duty to be cautious rests also on State courts. It is reciprocal.³

§ 1582. If State Court First Obtains Possession, It Retains Jurisdiction, Except in Three Instances.—Where property afterwards claimed by the bankruptcy trustee is taken into the custody of the State court (or any other court than the bankruptcy court) before the bankruptcy petition was filed, the State court, or such other court continues to retain jurisdiction over the entire matter except in three instances, later to be explained, and the only thing for the trustee to do is to get himself admitted as a party into the case in the State court and to litigate his rights there. For the rule of law that the Court first obtaining jurisdiction over the "res" retains it to the end, prevails in bankruptcy as well as in every other jurisprudence.⁴

3. In re Mustin, 21 A. B. R. 147, 165 Fed. 506 (D. C. Ala.).

4. *Pickens v. Dent*, 9 A. B. R. 47, 187 U. S. 177 (affirming 5 A. B. R. 644); In re Kavanaugh, 3 A. B. R. 832, 99 Fed. 928 (D. C. Ky.); *Marble Co. v. Grant*, 14 A. B. R. 288, 135 Fed. 322 (C. C. A. Penn.); *Nat'l Bk. of The Republic v. Hobbs*, 9 A. B. R. 190, 118 Fed. 626 (U. S. C. C. Ga.); compare, to same effect, under old law of 1867, In re Biddle, 9 B. Reg. 144; *Nat'l Bk. v. Moses*, 11 A. B. R. 772 (Sup. Ct. N. Y.); In re Shoemaker, 7 A. B. R. 437, 112 Fed. 648 (D. C. Va.): Even as to property levied on by execution within the four months. Instance, In re Heckman, 15 A. B. R. 500 (C. C. A. Wash.).

See analogously, the following cases cited and quoted under the proposition that "**Where the Bankruptcy Court has once assumed jurisdiction** over the property it has jurisdiction to determine all rights therein," etc., § 1795, et seq., affirming jurisdiction in the bankruptcy court, to be sure, but affirming it on precisely the same principle of the retention of jurisdiction by the court first obtaining possession of the res: In re McCallum, 7 A. B. R. 596, 113 Fed. 393 (D. C. Conn.); In re Whitener, 5 A. B. R. 198, 105 Fed. 180 (C. C. A. Tex.); *Turrentine v. Blackwood*, 4 A. B. R. 338, 28 So. Rep. 95 (Sup. Ct.

Ala.); In re Drayton, 13 A. B. R. 602, 135 Fed. 883 (D. C. Wis.); *Chauncey v. Dyke Bros.*, 9 A. B. R. 447, 119 Fed. 3 (C. C. A. Ark.); *Carter v. Hobbs*, 1 A. B. R. 215, 92 Fed. 594 (D. C. Ind.); In re Noel, 14 A. B. R. 720, 137 Fed. 694 (D. C. Md.); In re Huddleston, 1 A. B. R. 572 (Ref. Ala.); *Keegan v. King*, 5 A. B. R. 79, 96 Fed. 758 (D. C. Ind.); impliedly, *White v. Schloerb*, 4 A. B. R. 178, 178 U. S. 542; impliedly, In re Kellogg, 10 A. B. R. 8, 121 Fed. 333 (C. C. A. N. Y.); In re Rochford, 10 A. B. R. 615, 124 Fed. 182 (C. C. A. S. Dak.); In re Moody, 12 A. B. R. 724, 134 Fed. 628 (D. C. Iowa); In re Antigo Screen Door Co., 10 A. B. R. 359, 123 Fed. 249 (C. C. A. Wis.); In re J. C. Winship, 9 A. B. R. 641, 120 Fed. 93 (C. C. A. Ills.); In re Russell & Birkett, 3 A. B. R. 660, 101 Fed. 248 (C. C. A. N. Y.); In re Lemmon & Gale Co., 7 A. B. R. 291, 112 Fed. 296 (C. C. A. Tenn.); *Crosby v. Spear*, 11 A. B. R. 613, 98 Me. 542; In re Mertens, 12 A. B. R. 698, 131 Fed. 507 (D. C. N. Y.); In re Chambers, Calder & Co., 3 A. B. R. 537, 98 Fed. 865 (D. C. R. I.); In re Sentenne & Green Co., 9 A. B. R. 649, 120 Fed. 436 (D. C. N. Y.); *Leidigh Carriage Co. v. Stengel*, 2 A. B. R. 396, 95 Fed. 637 (C. C. A. Ohio); In re Rudnick & Co., 20 A. B. R. 33, 160 Fed. 903 (C. C. A. N. Y.), quoted at § 1585; In re New England Breeders' Club, 23

Eyster v. Gaff, 91 U. S. 521: "The opinion seems to have been quite prevalent in many quarters at one time, the moment a man is declared a bankrupt the District Court, which has adjudged, draws to itself, by that act, not only all control of the bankrupt's property and credits, but that no one can litigate with the assignee or contest rights in another court, except in so far as the Circuit Court took concurrent jurisdiction, and all other courts can proceed no further in suits of which they had, at that time, full cognizance, and it was a prevalent practice to bring any person who contracted with the assignee any matter growing out of disputed rights of property or of contracts into the bankrupt courts by the service of a rule to show cause, and to dispose of their rights in a summary way. This court has steadily set its face against this view. The debtor of a bankrupt, or the man who contests the right to real and personal property with him, loses none of these rights by the bankruptcy of his adversary. The same courts remain open to him in such contests, and the statute has not divested those courts of jurisdiction in such actions. If it has, for certain classes of actions, concurrent jurisdiction for the benefit of the assignee in the circuit and district courts of the United States, it is concurrent with and does not divest that of the State courts."

Peck v. Jenness, 7 How. (U. S.) 625: "These rules have their foundation, not merely in comity but on necessity. For if one court may enjoin, the other may retort by injunction; and thus the parties be without remedy; being liable to a process for contempt in one, if they dare proceed in the other. Neither can one take property from the custody of the other by replevin, or any other process, for this would produce a conflict extremely embarrassing to the administration of justice."

Metcalf v. Barker, 187 U. S. 173, 9 A. B. R. 36 (reversing *In re Lesser*, 5 A. B. R. and 3 A. B. R.): "The State court had jurisdiction over the parties and the subject matter and possession of the property; and it is well settled that where property is in the actual possession of the court this draws to it the right to decide upon conflicting claims to its ultimate possession and control. * * * A judgment or decree in enforcement of an otherwise valid pre-existing lien is not the judgment denounced by the statute, which is plainly confined to judgments creating liens. If this were not so the date of the acquisition of a lien by attachment or creditor's bill would be entirely immaterial."

Pickens v. Dent, 5 A. B. R. 644 (C. C. A. W. Va., affirmed in 9 A. B. R. 47, 187 U. S. 177): "Briefly stated, the rule is this: Considering the peculiar character of our government, and keeping in view the forbearance which courts of co-ordinate jurisdiction exercise towards each other, it follows that the court which first obtains rightful jurisdiction over the subject matter of a controversy must by all other courts be permitted to proceed therein to final judgment. The Federal courts will not interfere with the administration of affairs lawfully in the custody and jurisdiction of a State court, nor will they permit the courts of the State to interfere concerning litigation rightfully submitted to the decision of the courts of the United States. The Bankrupt Act of 1898

A. B. R. 689, 175 Fed. 501 (D. C. N. H.); *In re Rohrer*, 24 A. B. R. 52, 177 Fed. 381 (C. C. A. Ohio), quoted at § 1586.

Plaut v. Gorham Mfg. Co., 20 A. B. R. 269, 159 Fed. 754 (D. C. N. Y.); impliedly, *Murphy v. Hofman*, 211 U. S. 562, 21 A. B. R. 487, quoted at § 1796, et seq.

In re Munro, 28 A. B. R. 369, 197 Fed. 450 (D. C. N. Y.); *Bear Gulch, etc., Co. v. Walsh*, 28 A. B. R. 724, 198 Fed. 351 (D. C. Mont.); *Hobbs v. Head & Dowst Co.*, 26 A. B. R. 63, 185 Fed. 1006 (C. C. A. N. H.); *Hebert v. Crawford*, 228 U. S. 204, 30 A. B. R. 24, quoted at § 1796.

does not in the least modify this rule, but with unusual carefulness guards it in all of its detail, provided the suit pending in the State court was instituted more than four months before the District Court of the United States had adjudicated the bankruptcy."

Impliedly, *Carling v. Seymour Lumber Co.*, 8 A. B. R. 29, 113 Fed. 483 (C. C. A. Ga.): "A receiver or trustee, when appointed in the bankruptcy proceedings, while not entitled to the mortgaged property, will be entitled to any excess arising from the foreclosure sale, when made by order of the State court after the payment of the mortgages and costs of foreclosure. He will also be entitled, when appointed, to the possession of the choses in action and the other property in the hands of the State court's receiver which is not covered by the mortgages. The bankrupt law is equally binding on the State and the Federal court, and we cannot doubt that the former will, on proper application, give full effect to it. Where assets are in the hands of the receiver of one court which legally and equitably belong to the trustee or receiver appointed by another court, comity requires, as a general rule, that application should be made for a proper order to the former court, whose officer has possession of the property. This rule is reciprocal between the Federal and State courts, each respecting the possession of the other."

In *re English*, 11 A. B. R. 677, 127 Fed. 940 (C. C. A. N. Y., reversing 10 A. B. R. 133): "The situation, as we view it is this: Two parties claimed certain personal property as tenants in common, and sought the aid of the State court to determine their rights and to distribute the property or its proceeds. The state court, by its receiver, took possession of the corpus of the property, and converted it into money, which the receiver held to be distributed between the respective claimants when their rights should be determined. All this took place more than a year before petition in bankruptcy was filed. Indisputably, the state court had full jurisdiction of the parties, or the controversy, of the subject matter, and had reduced the property to its possession. We know of no provision of the Bankrupt Act, and our attention is called to no authority, which will sustain the proposition that, when a year afterwards one of the parties to the action is adjudicated a bankrupt, the state court is shorn of its jurisdiction to determine the controversy and must turn over the property to the bankruptcy court."

In *re Seebold*, 5 A. B. R. 364, 105 Fed. 910 (C. C. A. La.): "There is no provision in the present bankrupt law which authorizes or permits the courts of bankruptcy, by the use of either summary or plenary process, to stop the proceedings of the State court in a suit in which it had already, before the institution of the proceedings in bankruptcy, obtained possession of the subject matter and jurisdiction of the parties."

Compare, where the subject of the custody is real estate; *Frazier v. Southern Loan & Trust Co.*, 3 A. B. R. 710, 99 Fed. 707 (C. C. A. N. Car.): "The District Court seems to have been of the opinion, and it is the contention of counsel for the respondent in this court, that the receiver must be in the actual possession of the property in order to place it in the custody of the court. This position is erroneous. 'A court of equity, by its order appointing a receiver, takes the subject matter of the litigation out of the control of the parties and into its own hands, and ultimately disposes of all questions, legal or equitable, growing out of the proceeding.' High, Rec., § 4. As stated by the Supreme Court of Appeals of Virginia in *Beverly v. Brooks*, 4 Gratt. 187: 'A decree appointing receivers levies upon the property an equitable execution.' The possession of the receiver is that of the court, of which he is the ministerial officer. Thus it is that, inasmuch as the receiver is merely an officer of the court appointing him, property in his possession is said to be in the custody

of the law. * * * And it is said to be immaterial in this respect that the receiver appointed declines to act, the property being, notwithstanding, in the custody of the law.' Beach, Rec., § 221. Nor is it necessary for a court of equity to take possession of the property in litigation, or to attempt to do so by the appointment of a receiver, where the object of the suit is to set aside a fraudulent conveyance and enforce judgment liens against the land of the debtor."

In re Price & Co., 1 A. B. R. 606, 92 Fed. 987 (D. C. N. Y.): "This court, however, can make no order requiring the receiver in a State court to transfer the assets in his custody to the trustee in bankruptcy. The receiver is an officer of the State Court, the court had full jurisdiction of the action to dissolve the partnership, and under its authority the receiver became vested with the title for the purpose of that action, which included a distribution of the property among creditors. The Bankruptcy Act does, indeed, vest in the trustee the title to all the bankruptcy's property and rights of action whether legal or equitable (30 Stat. 565, § 70) but this does not authorize an interference by one court with the property lawfully in possession of another court of competent jurisdiction."

Linstroth Wagon Co. v. Ballew, 18 A. B. R. 28, 149 Fed. 960 (C. C. A. Tex.): "The features of this case call to mind the opinion which seems to have been quite prevalent in many quarters at one time, while the Bankruptcy Act of 1867 was in force, that the moment a man is declared bankrupt, the District Court, which has so adjudged draws to itself, by that act, not only all control of the bankrupt's property and credits, but that no one can litigate with the trustee contested rights in any other court except in so far as the Circuit Courts had concurrent jurisdiction, and that other courts could proceed no further in suits of which they had, at that time, full cognizance; as the result of which opinion the practice became prevalent to bring any person who contested with the trustee any matter growing out of disputed rights of property or contracts, into the Bankruptcy Court by service of the rule to show cause, and dispose of their rights in a summary way. Against this view of the matter and practice which for a time sweepingly prevailed, the Supreme Court steadily set its face. *Eyster v. Gaff*, 91 U. S. 525, 23 L. Ed. 403. On the going into effect of the present Act, some of the referees in bankruptcy and of the judges of those courts, unmindful of the teaching of the Supreme Court under the Act of 1867, or disregarding its lesson, began to follow the practice which had prevailed under that Act, against which the Supreme Court had steadily set its face. With the usual tendency toward the growing weight of precedents, that practice had extended and become widely prevalent before the case of *Bardes v. Hawarden Bank*, 178 U. S. 524, 4 Am. B. R. 163. * * * These amendments do not touch the case of the appellant. It does not claim the property here in controversy under any transfer from the bankrupt; it expressly disclaims being a creditor of the bankrupt at the time of the institution of this suit. The suit is not founded upon a claim from which a discharge in bankruptcy would be a release, and therefore is not subject to the provisions of § 11a. Before the filing of the involuntary petition, which imparted life to the jurisdiction of the Court of Bankruptcy as to Morgan and his estate, the appellant asserted its title to the specific personal property, clearly marked, branded, and distinctly pointed out, which it sought to recover against the bankrupt, then in possession of it, and obtained appropriate preliminary process for placing the property in safe custody pending the trial of appellant's title thereto. It did not seek to acquire or fix a lien by the levy of its writs of sequestration, or by the recovery of a judgment, but to establish its rights to the specific property and recover, lawfully, the possession of it. The appellant could not have sued in the Circuit Court, because the value of the property was less

than \$2,000; it could not sue in the United States District Court, because that court had no jurisdiction in civil cases, apart from its jurisdiction as a Court of Bankruptcy, and its jurisdiction as a Court of Bankruptcy had then not yet been vitalized by the filing of the involuntary petition. Therefore, it could invoke the jurisdiction of the proper State court only, which it did, and by its petition and the suing out of the writs for which it prayed, that court obtained jurisdiction of the cause and the jurisdiction was not lost, or in any way affected by the subsequent filing of the involuntary petition against Morgan, or by the subsequent adjudication that he was a bankrupt. The trustee might have obtained leave of the Court of Bankruptcy to appear and defend the suit, and have so appeared by leave of the State court; but he was not a necessary party, and whether he did so appear or not the suit could proceed to final judgment which would be binding on the trustee equally with any other party acquiring in interest *pendente lite*. Therefore, so far as the property itself or the admitted proceeds of that property are concerned, it is immaterial whether we consider that the trustee became or not, legally, a party to the litigation in the State court."

In *re Tune*, 8 A. B. R. 286, 115 Fed. 906 (D. C. Ala.): "When the only right of possession by the State court of attached property is based on an attachment lien, which is annulled by the adjudication in bankruptcy, the State court loses all jurisdiction of the rem, which is transferred into the exclusive jurisdiction of the court of bankruptcy. There is no longer any right of possession in the officer of the State court, who then holds as bailee for the person rightfully entitled to possession, and becomes a trespasser if he fails to deliver on proper demand.

"In cases of concurrent jurisdiction the court first obtaining possession of the property administers it, but where that court loses jurisdiction, and it is transferred by operation of valid laws to a court of the United States, which has exclusive jurisdiction of the subject matter, the question becomes one of the obedience to the paramount authority of the constitution, and comity can have no influence in determining the right."

In *re Gerdes*, 4 A. B. R. 346, 102 Fed. 318 (D. C. Ohio): "The State Court had jurisdiction of the subject matter and of the parties, and the control of the property for the purposes of sale, and it is clear under the authorities that it had power to proceed with the sale and the distribution of the proceeds thereof notwithstanding the commencement, pending the sale, of the proceedings in bankruptcy against Gerdes. Its jurisdiction was not ousted by the commencement of the proceedings in bankruptcy, and it has exclusive jurisdiction to determine and enforce the right of Pruden in the property or its proceeds."

Furth v. Stahl, 10 A. B. R. 442 (Sup. Ct. Penna.): "But independently of his acts or agreement the jurisdiction is clear. The court was distributing a fund in its own hands raised by it on its own process. Its authority to do so did not depend on any one's consent."

Inferentially, *Turrentine v. Blackwood*, 4 A. B. R. 339, 28 So. Rep. 95 (Ala.): "Conceding that the State and Federal Courts have concurrent jurisdiction in certain instances over the bankrupt's property, another principle is universally acknowledged, 'that when two courts have concurrent jurisdiction, that which first takes cognizance of the case, has the right to retain it, to the exclusion of the other; that if a trust estate is being administered by a court of competent jurisdiction, or when property is in *gremio legis* of a court of rightful jurisdiction, no other court can interfere and wrest from it the possession and jurisdiction first obtained.'"

Savings Bk. v. Jewelry Co., 12 A. B. R. 781, 123 Iowa 432: "At the time

of the adjudication in bankruptcy, the foreclosure proceedings were pending in the State court, and the mortgaged property was in the hands of a receiver appointed by the State court awaiting a determination of such proceedings. The adjudication in bankruptcy and the appointment of a trustee did not have the effect to abate the suit thus pending, or take away the right of the State court to decree and enforce a specific lien upon the property. That the enactment of the general bankruptcy law so far supersedes and suspends the operation of State insolvency laws as that a receiver or assignee in insolvency proceedings instituted under State statutes may be properly required to surrender possession to a trustee in bankruptcy, may be conceded. And such are the cases cited by counsel for appellant. But such doctrine cannot be extended to an action for the enforcement of a specific lien. Jurisdiction of such actions in the State court is not sought to be taken away by the Federal statute, and such could not well be. The action is not one to administer upon the estate of the bankrupt, or any portion of such estate. The purpose thereof is to ascertain if the plaintiff have a right to resort, by virtue of a specific lien claim, to the particular property in controversy, as against all other creditors or claimants, for the payment of his debt or the satisfaction of his demand. His right would be the same whether presented to the State or the Federal court in an action to foreclose, or by way of a claim made in the bankruptcy proceedings. Hence it is that the court which first takes jurisdiction and assumes control of the property retains it for all the purposes of a final order or decree. True, the trustee in bankruptcy may intervene in such action pending in the State court, as did this intervener, and be heard to contest the existence or the validity of the specific lien claimed, and he may well be awarded the property in the event the existence of the lien claimed is denied by the decree. But that a trustee may work an ouster of jurisdiction in the State court in such cases by pointing out the pendency of the bankruptcy proceedings has no support in reason or well-considered authority."

In *re* Greater Amer. Expo., 4 A. B. R. 486, 102 Fed. 986 (C. C. A. Tenn.): "We are of the opinion that the bankrupt court had no right to stay the suit to enforce the lien as against the res in the possession of a third party, to wit, the wrecking company, although the trustee of the bankrupt was incidentally interested in the amount of the lien which might be established, by virtue of the contract which the bankrupt had entered into with the vendee."

Taylor v. Taylor, 4 A. B. R. 217, 59 N. J. Eq. 84 (N. J. Ch.): "The policy of the Federal Supreme Court seems to have been to permit any such suit, which was pending in a State court at the time when bankruptcy proceedings were begun, to proceed to final settlement."

It has been held, but erroneously, that the bankruptcy court will have exclusive jurisdiction in any case where property has been sequestered by a state court within the four months.⁵

5. In *re* Knight, 11 A. B. R. 1, 125 Fed. 35 (D. C. Ky.): But in this case the receivership operated to do more than simply to keep custody of property covered by the pre-existing valid lien and so the case was rightly decided though on grounds too broadly stated.

Possession under Writ of General Execution Different.—It has been held that the possession of a sheriff, marshal or constable under writ of gen-

eral execution does not give jurisdiction to the court over the rem, at least not in the sense in which such officer holds possession where the sale is a judicial sale as distinguished, from an execution sale and such officer therefore may be required to surrender custody, even though the lien of the levy is not nullified by the bankruptcy, the lien following the property.

In *re* Vastbinder, 13 A. B. R. 148, 132 Fed. 718 (D. C. Penn.): "While

In re Kaplan, 16 A. B. R. 268, 144 Fed. 159 (D. C. Ga.): "Of course, the mortgage lien of Mrs. Herndon, if valid, and I do not understand that to be questioned, is in no way affected by the property going into the hands of the trustee in bankruptcy. * * * Counsel rely on the case of *Metcalf v. Barker*. * * * The effect of this decision of the Supreme Court is discussed by judge Evans in the recent case of *In re Knight*. * * * It is his conclusion that neither that case nor the case of *Pickens v. Roy* [*Pickens v. Dent*] affects the present question; and this is in accordance with my own views on the subject. * * * Reference to that case is sufficient. It may be proper to call attention

the lien of the levy, if it has been properly kept up, is not divested by the present proceedings, antedating as it does over four months, it is not necessary to its preservation or enforcement, that the goods should be actually disposed of by the sheriff on the vend. ex. The trustee took subject to the levy and the execution creditor will be entitled to be paid out of the proceeds realized from the goods without regard to who may happen to sell them. But bankruptcy having intervened, jurisdiction over the property of the bankrupt has been drawn to this court under the direction of which the estate is to be now administered, and to this forum parties, who have claims thereon by way of lien or otherwise, are remitted for the ascertainment and establishment of their rights. There is no valid reason why in disregard of this the trustee should be compelled to follow the fund arising from the goods, elsewhere, and it would reverse the natural order and complicate matters to require him to do so. The case of *Metcalf v. Barker*, 187 U. S. 165, 9 Am. B. R. 36, on which reliance is placed, was different. That was a creditor's bill by which not only did the complainant secure a specific lien, but the court in which it was filed obtained direct jurisdiction over the property against which the equity was asserted; and it was with reference to that situation that the bankruptcy proceedings were held to have no effect. But in the present instance the goods are not under the dominion of another court. They have simply been taken by the sheriff upon process as an officer of the law, the same as they might be by a constable on an execution from a magistrate or a bailiff under landlord's warrant on a claim for rent. Surely in the latter, the trustee should not be subjected to the uncertainties of a justice's court or the irresponsible action of a landlord, and if not why should he any more give way to an execution in the hands of the sheriff?

"The petition is therefore sustained

and the writ of vend. ex. in the hands of the sheriff stayed."

In re Baughman, 15 A. B. R. 23, 138 Fed. 742 (D. C. Penn.): "In the present instance, while the execution creditor by virtue of its judgment has a lien upon the real estate proposed to be sold, which, antedating the bankruptcy proceedings by over four months as it does, may not be affected thereby, yet, bankruptcy having intervened, the sale and distribution of the property as well as the establishment of the correct amount due to the judgment creditor which seems to be in dispute, belongs to this court, unless it seems best to let it go on elsewhere, as might be the case if the liens were more than enough to exhaust the property leaving nothing for general creditors, although this is not always controlling and is entirely optional. In re Keet, 11 A. B. R. 117. A stay of execution does not interfere with the lien, as argued; it merely controls its enforcement, in the interest of general creditors where that is deemed advisable. Neither is there any difference in this respect between real and personal property."

In re Booth, 2 A. B. R. 770, 96 Fed. 943 (D. C. Ga.). See post, "Summary Orders on Court Officers Holding under Nullified Legal Liens," § 1827, note.

The State Court will be deemed to have custody of the rem, at any rate where it is real estate, if a receiver has been appointed by it although such receiver has failed to reduce the property to actual possession, or has for a long time neglected to take any steps in relation thereto, *Frazier v. Southern Loan & Trust Co.*, 3 A. B. R. 710, 99 Fed. 707 (C. C. A. N. Car., reversing *Southern Loan & Trust Co. v. Benbow*, 3 A. B. R. 9).

Adverse Claimant Himself Becoming Bankrupt.—Where the adverse claimant himself becomes bankrupt the bankruptcy court, of course, obtains jurisdiction, *In re Rosenberg*, 8 A. B. R. 624, 116 Fed. 402 (D. C. Penn.).

particularly to the fourth headnote in the Knight case, especially pertinent here, which is as follows: 'In general, an adjudication of bankruptcy vests the bankruptcy court with exclusive jurisdiction to administer the property of the bankrupt, as against any State court which may have obtained possession of such property through proceedings instituted within four months prior to the adjudication, and it is immaterial that the proceedings in the State court were for the enforcement of liens not affected by the Bankruptcy Act.'

And in one case it was held that where, within the four months period, an action to enforce a lien was brought in a state court against a bankrupt, its entire property being involved in the litigation, the bankruptcy court had jurisdiction to stay further proceedings in the action, and, if necessary, to take charge of the property and to supersede the custody of the State court.

Coal Land Co. v. Ruffner, 21 A. B. R. 474, 165 Fed. 881 (C. C. A. W. Va.): "In the case here the whole proceeding in the State court was within four months of the time both of the filing of the petition in bankruptcy and of the adjudication, and the entire property of the bankrupt was involved in the litigation. The District Court, therefore, had the jurisdiction, and the right to assert it, to stay further action by the State court, and if necessary to secure a just and equitable distribution of the bankrupt's estate to take charge of the property to this end. The powers of the District Court in bankruptcy are ample to administer an estate with due regard to priorities or vested liens and to protect all interests in such estate, whether they be legal or equitable." This case further quoted at §§ 1603, 1902.

The rule, however, is stated in the case of *Coal Land Co. v. Ruffner* in broader terms than the facts necessitated, for the facts showed the case to be that of a lien created by legal proceedings within four months rather than that of legal proceedings within four months merely enforcing good and valid pre-existing liens.⁷

And it was held in one case that even where a foreclosure suit had been started before the bankruptcy, but within four months thereof, and the bankruptcy court afterwards obtained actual possession of the property involved, it had jurisdiction to marshal the liens, to determine all rights in the property, and to enjoin the further prosecution of the foreclosure suit, though there was no claim that the liens were preferential or otherwise invalid.⁸ In this case, however, the state court receiver had voluntarily surrendered possession to the trustee.

The rule is laid down in some cases even more strictly against the bankruptcy court than in the main proposition, to the following effect: Where property afterwards claimed by the trustee is taken into the custody of the state court even after the filing of the petition, but before adjudication and before any bankruptcy officer actually takes possession or any restraining order is applied for the state court continues to retain jurisdiction over the res except in the three instances named, and the only recourse of the

7. See ante, § 1444; post, § 1586.

8. In re Dana, 21 A. B. R. 684, 167 Fed. 529 (C. C. A.).

trustee is to get admitted as a party into the case in the State Court, if permitted, and to litigate his rights there.

In *re Wells*, 8 A. B. R. 75, 114 Fed. 222 (D. C. Mo.): "All agree that the court, State or Federal, which first takes possession of the property, retains the possession and the jurisdiction. This is elementary, and cases need not be cited to emphasize the proposition. But the trustee, by counsel, argues that the 'possession' does not mean physical possession. This court, by any of its officers, never has had physical possession of the property. And the decision of this question requires a construction of the bankrupt statute of 1898. Counsel for the trustee insists that the mere filing of the petition in involuntary bankruptcy is notice to the world, and no other court must interfere with any property then in the possession of the bankrupt, and that any subsequent interference by a State court is avoided and nullified by the subsequent adjudication of bankruptcy of the debtor. I decline to so hold, and for reasons which seem to me conclusive. Conflicts between courts over the same property should at all times be avoided, if possible, because at times such conflicts are unseemly. The mistake is constantly being repeated, and sometimes by lawyers, by asserting that the United States courts are greater and more commanding than the State courts. I cannot agree to this. The State courts are courts of general jurisdiction, while a Federal court is one of limited jurisdiction. Of course when a Federal court once acquires jurisdiction, then such jurisdiction becomes complete. And it is true that on some questions the Federal courts have exclusive jurisdiction—such as in admiralty and other cases. Under some of the old bankruptcy statutes such has been the case. But it is not so under the act of 1898."

And this rule, in still other cases, is held even to apply—at the discretion, however, of the bankruptcy court—where the suit is started in the state court after adjudication;⁹ and in still other cases is even held to apply where the trustee claims the liens involved are nullified by the peculiar provisions of the Bankruptcy Act itself against preferences, both where the cases are started before the bankruptcy.¹⁰

Savings Bk. v. Jewelry Co., 12 A. B. R. 781, 123 Iowa 432: "His rights would be the same whether presented to the State or Federal court in an action to foreclose, or by way of a claim made in the bankruptcy proceedings."

And also where started after the bankruptcy.

Heath v. Shaffer, 2 A. B. R. 98, 93 Fed. 147 (D. C. Iowa): "He should appear in the State Court, and, by pleading the adjudication in bankruptcy and his appointment as trustee, lay the foundation for the protection of his rights. If he questions the jurisdiction of the State court, he can plead thereto in proper form. If the case be one that is removable under the provisions of the Judiciary

9. In *re Porter*, 6 A. B. R. 259, 111 Fed. 892 (D. C. Ky.); In *re San Gabriel Sanatorium Co.*, 7 A. B. R. 206, 109 Fed. 111 (C. C. A. Calif.); *Heath v. Shaffer*, 2 A. B. R. 98, 93 Fed. 647 (D. C. Iowa).

10. Impliedly, *Furth v. Stahl*, 10 A. B. R. 442 (Pa. Sup. Ct.). Perhaps, also, *Marble Co. v. Grant*, 14 A. B. R. 288, 135 Fed. 322 (C. C. A. Penn.):

wherein the court held that where prior to the filing of a petition against an involuntary bankrupt a creditor had brought an attachment suit in a State court, to enforce an asserted right in rem, under the State law the bankruptcy court was without jurisdiction of the res. But in this case it does not appear whether the attachment suit was begun within the four months or not.

Act, he can make the requisite showing. If he does not dispute the validity of any lien asserted by the plaintiff, he can set up his title and rights as trustee, subject to the admitted lien, and the State court will protect his rights in the premises. If he wishes to contest the validity or extent of the adverse claim asserted by the plaintiff in the State court, he can do so by answer or cross bill. If, upon the hearing, the State court holds and adjudges the plaintiff's claim or lien to be invalid and void either at the common law or under the provisions of the Bankrupt Act, that court would, undoubtedly order the property to be delivered to the possession of the trustee. If the State court holds and adjudges the lien of the plaintiff to be valid, it would, upon the proper showing, also recognize the title and rights of the trustee, subject to the lien of the plaintiff, and would enforce the same according to the true intent and meaning of the Bankrupt Act. In some of the discussions had upon this general subject, it seems to be assumed that the State courts cannot aid in carrying out the general provisions of the Bankrupt Act, and that the trustee can only appeal to the courts of bankruptcy when seeking to secure a disposition of a bankrupt's estate under that act; but this is a mistaken view of the law. The State courts, in all proceedings pending before them, have the right to apply and enforce the provisions of the Bankrupt Act in the determination of the questions at issue before them, and can give full protection to the rights of the trustee. The Bankrupt Act is the law of the land, and the State courts have full right to enforce its mandate in all proceedings properly before them. Of course, it is not meant by this that a State court can adjudge a person to be bankrupt, or grant him a discharge, or control the distribution of the bankrupt's estate; but what is meant is that in all suits pending before them, wherein may be involved a contest between the trustee and a third party, which depends, in whole or in part, upon the provisions of the Bankrupt Act, the State courts must, of necessity have full right and jurisdiction to apply and enforce the provisions of the Bankrupt Act, not only in deciding the question of right at issue, but in securing to the parties the proper protection accorded to them under the act. Thus, in the proceedings pending in the State court, even though the court should adjudge the lien of the mortgage to be valid, it would undoubtedly recognize and properly protect the right of the trustee in the mortgaged property, and in ordering a sale of the property would have due regard to the rights and equities of the mortgagees and the trustee alike. Taking into consideration the entire provisions of the act, it clearly appears that it was the intent of Congress to utilize the State as well as the Federal courts in administering the law, at least in cases wherein an adversary claim may exist between the trustee and third parties."

And, in still other cases, the rule is broadly stated to be that neither plenary nor summary process from the courts of bankruptcy will lie to stay proceedings in a state court nor to order the surrender of property thereby, even though possession has been acquired by the state court within four months of the bankruptcy.¹¹

However, it has been held that where, during the pendency of an insolvency petition, a receiver is appointed, but, between the entry of the decree appointing him and the filing of his bond, an officer of the state court takes possession of the goods of the alleged bankrupt found on the premises

11. In re Seebold, 5 A. B. R. 358 (C. C. A. La.); Marble Co. v. Grant, 14 A. B. R. 288, 135 Fed. 322 (C. C. A. Penn.).

of the bankrupt, under writ of replevin, such seizure is an unauthorized interference with the possession of the bankruptcy court.

In *re Alton Mfg. Co.*, 19 A. B. R. 805, 158 Fed. 367 (D. C. R. I.): "The goods were seized while in the basement of the Alton Company's mill, and in the possession of said company or its assignees. The act of bankruptcy charged in the creditor's petition was the making of a general assignment for the benefit of creditors. The Supreme Court of Rhode Island has held that an action of replevin in that State is so far a proceeding in rem that, unless the res has actually been taken possession of by the officer, there is nothing before the State court, and the court is without jurisdiction to decide the question of title. *Warren v. Leiter*, 24 R. I. 36, 39, 52 Atl. 76. If jurisdiction was acquired by the State court, it was not earlier than the time of seizure, about 11 o'clock a. m. We need not consider, therefore, whether the writ was sued out before the filing of the petition in bankruptcy, nor pass upon the petitioner's contention that the bankruptcy court acquired jurisdiction of the goods by the mere filing of an involuntary petition. See *In re Weinger, Bergman & Co.* (D. C.), 11 Am. B. R. 424, 126 Fed. 875. It is enough to inquire whether the bankruptcy court had possession at any time before the seizure in replevin. It is true that the receiver had not filed his bond, nor taken actual possession, but the terms of the decree appointing him were positive: 'It is ordered and decreed that Henry R. Segar of said Westerly be and he is hereby appointed receiver of the goods, chattels, property and effects of the Alton Manufacturing Company,' and, though he was required to give bond, his appointment dated from the entry of the decree, and preceded the seizure in replevin. The entry of this decree, in my opinion, conferred upon the bankruptcy court such jurisdiction of the goods of the bankrupt that a subsequent seizure under a writ of replevin from the State court was unauthorized, and an interference with the possession of the bankruptcy court. *White v. Schloerb*, 178 U. S. 542, 4 Am. B. R. 178. * * * It is true that in that case there had been an adjudication of bankruptcy, and the entrance to the bankrupt's store had been locked by order of the referee before the seizure. In the present case there had been no adjudication of bankruptcy, and no act of the receiver amounting to an actual taking of possession. For the preservation of the estate, however, a decree appointing a receiver had been entered; and, considering the nature of this decree, it seems to be unnecessary that it should have been followed by an actual seizure by the receiver in order to confer prior jurisdiction on the bankruptcy court. * * * This jurisdiction attached irrespective of the assignment made by the Alton Company for the benefit of creditors, for the rule is the same whether the goods are held by the bankrupt or for him. In *Bryan v. Bernheimer*, 181 U. S. 192, 193, 5 Am. B. R. 623, * * * it was said that an assignee under a general assignment for creditors is an agent of the bankrupt for the distribution of the proceeds of his property."

On the other hand, going to the opposite extreme, "a certain revisory power" over suits in the state courts was claimed for the bankruptcy courts in one case¹² even though the particular suit in question was merely one to foreclose a mechanic's lien and had been commenced more than four months before the filing of the bankruptcy petition, the cause of

¹². *Hobbs v. Head & Dowst Co.*, 26 A. B. R. 63, 185 Fed. 1006 (C. C. A. N. H.).

the advancing of this novel and somewhat indefinite doctrine being that "It was only by the grace of the State Supreme Court that the final judgment was delayed and a hearing of any kind given the trustee." It would seem to have been error, though, for the state court not to have granted a hearing to the trustee, who was the successor to the bankrupt, in behalf of creditors, of which error he might have taken advantage. Any such doctrine, however, of latent "revisory power," "certain" or uncertain, is unsound. The case (*In re Dana*, 21 A. B. R. 683, 167 Fed. 529) was one where the state court receiver had voluntarily surrendered possession of the assets to the bankruptcy court, which presents an entirely different proposition.

The true rule, however, is that stated at the beginning of this section.

§ 1583. Simply because Bankruptcy Court Preferable or Trustee Interested, Not Sufficient to Confer Jurisdiction.—Simply because the bankruptcy court can better settle and adjust the rights of the parties, is not sufficient to confer jurisdiction on it under the present law;¹³ nor because the trustee is interested.

In re Greater Amer. Exp., 4 A. B. R. 486, 102 Fed. 986 (C. C. A. Neb.): "The fact that a trustee in bankruptcy may be interested in the result of a litigation which is pending between third parties in a State court does not entitle him to have the proceedings in such action stayed, as between such third parties, and to have the controversy transferred for adjudication to the bankrupt court."

§ 1584. But State Courts May Be Permitted to Retain Jurisdiction Where Better Suited to Adjust Rights, Even Where Bankruptcy Court Might Have Jurisdiction.—But it is true the state courts may be permitted to retain jurisdiction in cases where the bankruptcy courts might assume jurisdiction, but do not do so because the rights of the parties can be better settled in the state courts.¹⁴

Compare, *Hooks v. Aldridge*, 16 A. B. R. 665, 145 Fed. 865 (C. C. A. Tex.): "While it is unquestionable that the federal courts are the final arbiters to settle

13. But compare decisions under the law of 1867, cited in editor's note to *Keegan v. King*, 3 A. B. R. 79 (D. C. Ind.).

In re Rudnick & Co., 20 A. B. R. 33, 160 Fed. 903 (C. C. A. N. Y.), quoted at § 1585; *Sample v. Beasley*, 20 A. B. R. 164, 158 Fed. 606 (C. C. A. La.). Also, compare, *In re United States Graphite Co.*, 20 A. B. R. 573, 159 Fed. 300 (D. C. Pa.), wherein the court held the lien to be good because it antedated the four months period, but nevertheless ordered a sale in bankruptcy clear of all liens, notwithstanding the possession of the sheriff under the levy, the court applying the well-known rule as to selling clear from liens, although here the bankruptcy court was not in possession.

14. See post, § 1794, et seq., subject of Bankruptcy Courts assuming jurisdiction. Instance, *Orr v. Tribble*, 19 A. B. R. 849, 158 Fed. 897 (D. C. Ga.); *In re William Openhym & Sons v. Blake*, 157 Fed. 536, 19 A. B. R. 639 (C. C. A. Mo.); inferentially, *Blake, trustee, v. Openhym & Sons*, 23 A. B. R. 616, 216 U. S. 322, quoted on other points, at § 3028; *In re New England Breeders' Club*, 23 A. B. R. 689, 175 Fed. 501 (D. C. N. H.); *Virginia, etc., Co. v. Olcott*, 28 A. B. R. 321, 197 Fed. 730 (C. C. A. N. C.); *In re Zehner*, 27 A. B. R. 537, 193 Fed. 787 (D. C. La.). Also, see note to *Keegan v. King*, 3 A. B. R. 79 (D. C. Ind.), for decisions under law of 1867.

questions arising under the bankruptcy laws, there are questions relating to comity and procedure, in the event of conflict of opinion between the State courts and the bankruptcy courts as to the possession of the bankrupt's assets, which remain unsettled by decision of the Supreme Court. Whether the bankruptcy courts should make such orders as will preserve the estate, and await the final result of the litigation in the State court, or should act on its own opinion of the want of jurisdiction of the State court, and enforce its order to secure the possession of the property, is one of the questions left unsettled, so far as we are advised, by a decision of the Supreme Court."

In *re United Wireless Tel. Co.*, 28 A. B. R. 394, 202 Fed. 896 (D. C. N. Y.): "Undoubtedly the very existence of any federal court does presuppose that State courts will not be free from local bias, but it is one thing to provide means to litigate for avoiding that bias, and another to intervene for that reason in the very operation of a court already begun. Even the latter power does exist (*Re Hecox*, C. C. A. 8th Cir., 21 A. B. R. 314, 164 Fed. 823; *Hooks v. Aldridge*, C. C. A. 5th Cir., 16 A. B. R. 658, 145 Fed. 865; *New Coal and Land Co. v. Ruffner*, C. C. A. 4th Cir., 21 A. B. R. 474, 165 Fed. 881) but its existence does not mean it ought always to be exercised, and in fact it ought to be very sparingly exercised, rather after the analogy of habeas corpus. *Ex parte Royall*, 117 U. S. 250.

"Indeed nothing more quickly makes contempt for law than to have judges each catching at jurisdiction, and nothing more quickly breeds confidence, than if judges really trust in each other. It shows rather a martial than a judicial vigor to assert such a jurisdiction, and unless it be unavoidable it ought not to be used. This is what the Supreme Court had in mind, I think, in *Re Watts*, 190 U. S. 1, 10 Am. B. R. 113, 23 Sup. Ct. 718, when it said, at page 35 of 190 U. S., at page 132 of 10 Am. B. R.: 'It remained for the State court to transfer the assets, settle the accounts of its receiver and close its connection with the matter. Errors, if any, committed in so doing could be rectified in due course and in the designated way.'

"Moreover, even if the State court does not so scrupulously regard the limitation of its own jurisdiction as the trustees think it should, they have their appeal, and if by evil chance, that does not serve them, still, since the question is of jurisdiction, the bankruptcy court has an inherent power to protect its own possession and its own suitors, should they be disturbed.

"The trustees complain of the expense of the defense, but I cannot avoid that, for it is an expense which arises from the financial entanglements of the bankrupt before bankruptcy. Besides, it ought not to be laborious or expensive to try the cause, in which they have no interest in the issues, but only in the form of the power to close up its own suit and enter a judgment. I could not, even if I would, enjoin such action, because it was possible that it might press its judgment further than it should. No case goes to that length."

The jurisdiction of the state court is not ousted merely because one of the defendants, in an action pending therein, has been adjudged bankrupt; and, in the absence of a restraining order, such action may be prosecuted to judgment.¹⁵

Indeed, an action brought by the trustee in the bankruptcy court to recover an alleged preference may be stayed for a reasonable time to await the decision of the state court in a suit therein pending, and in which the trustee has intervened, involving the same questions.¹⁶

15. *Friedman v. Zweifler*, 27 A. B. R. 412 (Sup. Ct. N. Y.).

16. *Davis v. The Planters' Trust Co.*, 28 A. B. R. 495, 196 Fed. 970 (D. C. Ky.).

§ 1584½. Or Bankruptcy Court May Surrender Custody.—Or the bankruptcy court may surrender custody to the state court or to the admiralty court, where the rights of the parties can be better settled there.¹⁷ Thus, in case of dower,¹⁸ or of maritime liens.¹⁹

But the assets thus surrendered will come into the other court burdened with the costs and expense of the bankruptcy court for their preservation.²⁰

§ 1585. Replevin and Other Suits Asserting Ownership, Where Seizure Made First by State Court, Not Abated.—A replevin suit or other action brought under claim of ownership of the property involved, in which property is seized before the marshal, receiver or trustee in bankruptcy takes possession, or any restraining order is issued, is not abated; and the state court retains jurisdiction.²¹

In *re Rudnick & Co.*, 20 A. B. R. 33, 160 Fed. 903 (C. C. A. N. Y., reversing 18 A. B. R. 750, 158 Fed. 223): "The plaintiffs, in replevin, on the contrary, allege that they were induced to sell the property to the bankrupt by false and fraudulent representations and that the title never passed to the bankrupt. * * * The argument of convenience and expediency is not properly before us, but it cannot be denied that a question which involves the title to property can, to say the least, be determined as well in a plenary suit, where witnesses are seen, examined and cross-examined, as in a summary proceeding based solely upon affidavits. There is no form of action known to the common law in which the rights of both parties can be safe-guarded so thoroughly as in an action of replevin. The jurisdiction of the District Court is purely statutory and unless the Bankruptcy Act permits the taking of property from a state official holding it under process duly issued, the right to do so cannot be maintained. It is contended that § 67f of the act, invalidating levies, judgments, attachments and liens obtained within four months against a person who is insolvent and providing that the property so affected shall pass to the trustee as part of the estate of the bankrupt, vests the necessary power in the District Court. We cannot accede to this view. It is manifest that the section in question deals with the property of the bankrupt. Assuming that Congress might lawfully pass a law requiring the property of third parties, found in the possession of the bankrupt, to be turned over to his trustee as part of his estate; it is sufficient for the purposes of this review that Congress has not done so in the present act. If A leaves his coat with B to be repaired and B refuses to return it, A can reclaim it in an action of replevin, and the status of that suit is not affected by the fact that B subsequently becomes a bankrupt. The mere assertion by B of ownership in the coat does not oust the court of jurisdiction and transfer the controversy to the bankrupt court. It presents a question of fact merely, to be tried in the court first obtaining possession of the property. The distinction between a requisition in replevin and a lien created by levy or

17. In *re Hughes*, 22 A. B. R. 303, 170 Fed. 809 (D. C. N. J.).

18. See post, §§ 1972, 1973. But compare, § 1813.

19. In *re Hughes*, 22 A. B. R. 303, 170 Fed. 809 (D. C. N. J.).

20. In *re Hughes*, 22 A. B. R. 303, 170 Fed. 809 (D. C. N. J.).

21. *Linstroth Wagon Co. v. Ballew*, 18 A. B. R. 28, 149 Fed. 960; *Pub. Co.*

v. Hutchinson Co., 17 A. B. R. 425 (Sup. Ct. Mich.); compare, inferentially, In *re Neely*, 7 A. B. R. 312, 112 Fed. 210 (C. C. A. N. Y.); In *re William Openhym & Sons v. Blake*, 157 Fed. 536, 19 A. B. R. 639 (C. C. A. Mo.); inferentially, *Blake, trustee, v. Openhym & Sons*, 216 U. S. 322, 23 A. B. R. 616, quoted at § 3028.

attachment is that the former deals primarily with the property of the plaintiff in replevin and the latter with the property of the bankrupt. It is of no moment that the title is in dispute. This is true in every contested replevin suit, and it is this question which the court must determine before judgment can be rendered."

In *re Wells*, 8 A. B. R. 75, 114 Fed. 222 (D. C. Mo.): "The question therefore is, does the filing in this court of a petition in involuntary bankruptcy, of itself, and before any order is made by this court, give this court jurisdiction of all the property then in the possession of the bankrupt, whether by him owned or not? And if the bankrupt then has possession of the property, but not owned by him, or the question of ownership is disputed, must the claimant have the question of ownership adjudicated by this court, and to the exclusion of the State court, which has taken possession of the property for adjudication?"

"All agree that the court, State or Federal, which first takes possession of the property, retains the possession and the jurisdiction. This is elementary, and cases need not be cited to emphasize the proposition. But the trustee, by counsel, argues that the 'possession' does not mean physical possession. This court, by any of its officers, never has had physical possession of the property. And the decision of this question requires a construction of the bankrupt statute of 1898. Counsel for the trustee insists that the mere filing of the petition in involuntary bankruptcy is notice to the world, and no other court must interfere with any property then in the possession of the bankrupt, and that any subsequent interference by a State court is avoided and nullified by the subsequent adjudication of bankruptcy of the debtor. I decline to so hold, and for reasons which seem to me conclusive. Conflicts between courts over the same property should at all times be avoided, if possible, because at times such conflicts are unseemly. The mistake is constantly being repeated, and sometimes by lawyers, of asserting that the United States courts are greater and more commanding than the State courts. I cannot agree to this."

(*William*) *Openhym & Sons v. Blake*, 19 A. B. R. 639, 157 Fed. 536 (C. C. A. Me.): "Upon learning of the fraud practiced upon them, the appellants promptly rescinded the sale. The bankrupt's entire stock of goods was then in the possession of a receiver appointed by a State court. He was engaged in selling it. Certain creditors of the bankrupt had six days previously filed a petition in bankruptcy, but no injunction against the continued sales was obtained, no receiver in bankruptcy was appointed, and no adjudication was had until a month afterwards. The rescission was properly effected by the assertion of appellants' purpose, the demand of the State court receiver for possession, and the replevin action begun with the permission of the State court. The right of rescission was not affected by the pendency of the bankruptcy proceedings."

Contra, In *re Weinger, Bergman & Co.*, 11 A. B. R. 424, 126 Fed. 875 (D. C. N. Y.): "Moreover, in this case, in my opinion, no question can arise which is based on the theory that the State court first obtained jurisdiction. The petition in bankruptcy was filed in this court and notice of it was given to the marshal about the time that the marshal arrived at the bankrupt's store, and before the goods were actually seized and taken away. Under the present Bankrupt Act, as under the Act of 1867, the filing of a petition in bankruptcy is a caveat to all the world, and in effect an attachment and injunction (*Mueller v. Nugent*, 184 U. S. 1, 7 Am. B. R. 224); and I think that when a petition is filed before a State court acts, the State court cannot, by any subsequent action, claim to have first taken possession of the res. The fact that the bankruptcy court may not have yet made an adjudication, and that no receiver or trustee has yet been appointed, in my opinion, is immaterial. The bankrupts' property

is within the jurisdiction of the bankruptcy court as soon as the petition is filed, so far as to prevent a State court which subsequently seizes the property from being held to have first obtained exclusive jurisdiction."

Also, *contra*, *In re Hymes Buggy & Implement Co.*, 12 A. B. R. 477, 130 Fed. 977 (D. C. Mo.): "True it is that the term 'all levies' would ordinarily in practice apply to a seizure under execution for the collection of money on a judgment. But looking at the connection and the whole statute, it is difficult to escape the conclusion that Congress employed the term 'all levies' in its most comprehensive sense, covering any and all seizures of property of the bankrupt within the four months period, under legal process, looking to the enforcement of claims against the bankrupt which would be released by his final discharge. Why nullify judgments, attachments, or other liens 'against a person who is insolvent, at any time within four months prior to the filing of a petition in bankruptcy against him,' and yet leave the claimant free to seize the property of the insolvent under replevin process?" But this case was wrongly reasoned. The assertion of ownership is not the assertion of a lien on the bankrupt's property but a denial that the property is the bankrupt's property; and it does not come within the mischiefs against which the Bankrupt Act was directed. In this particular case it appears the replevin suit was simply a cover and not the assertion of a bona fide claim of ownership. It was really an attempt to make replevin take the place of attachment.

However, it has been held that if the seizure in replevin was made after the appointment of the receiver but before the filing of his bond, and was a seizure from the possession of the bankrupt, it would constitute an unwarranted interference with the custody of the bankruptcy court.²²

§ 1586. Foreclosure and Other Suits Not Themselves Creating Liens Nullified by Bankruptcy, but Simply Enforcing Liens, etc., Not Abated, Where Started before Bankruptcy.—A suit in equity, such as a foreclosure suit or other legal proceedings to enforce a lien which itself is not claimed to be in contravention of the peculiar provisions of the bankruptcy act nullifying liens obtained by legal proceedings, where such suit or other proceedings is instituted before the filing of the bankruptcy petition, is not abated and the state court retains jurisdiction. It is not to be transferred to the bankruptcy court simply because the bankruptcy of the mortgagor or debtor occurs within four months of the commencement of the foreclosure suit.²³

²². *In re Alton Mfg. Co.*, 19 A. B. R. 805, 158 Fed. 367 (D. C. R. I.), quoted at § 1582. Compare, collaterally, limitations, ante, § 1121.

²³. *Eyster v. Gaff*, 91 U. S. 521, quoted supra. *In re Greater American Exposition*, 4 A. B. R. 486, 102 Fed. 986 (C. C. A. Tenn.), quoted supra. *Woods v. Klein*, 22 A. B. R. 722, 223 Pa. St. 251, quoted at § 1444; *In re New England Breeders' Club*, 23 A. B. R. 689, 175 Fed. 501 (D. C. N. H.). See note to *Keegan v. King*, 3 A. B. R. 79, 96 Fed. 758, for cases under law of 1867.

Reed v. Equitable Trust Co., 8 A. B. R. 242 (Sup. Ct. Ga.): "Unless the lienholder prove his claim as a creditor in the bankruptcy proceedings."

Obiter, *Leidigh Carriage Co. v. Stengel*, 2 A. B. R. 383, 95 Fed. 637 (C. C. A. Ohio). *Carling v. Seymour Lumber Co.*, 8 A. B. R. 29 (C. C. A. Ga.): "In this case a receiver had been appointed in the State court to take charge of the mortgaged property and also of all other property of the debtor, the petition being framed so that it stated a case not only for throwing the debtor into insolvency under the State Insol-

In *re Kane*, 18 A. B. R. 594, 152 Fed. 587 (D. C. N. Y.): "As to the second motion, in which a stay of the sale under the foreclosure is asked, a hasty examination seems to indicate, from the reasoning set forth in the case of *Metcalf v. Barker*, 187 U. S. 165, 9 Am. B. R. 36, that the judgment in foreclosure has not created the lien, and is not within the provisions of § 67f. The judgment is merely a decree by a court having competent jurisdiction directing the enforcement of a lien which cannot be affected or vacated by bankruptcy proceedings."

In *re Rohrer*, 24 A. B. R. 52, 177 Fed. 381 (C. C. A. Ohio): "The mortgage lien of Hofer was obtained long prior to a period of four months next preceding the date of filing of the petition in bankruptcy against Rohrer; and while the suit was commenced and the decree of foreclosure rendered within that period, neither the mortgage lien nor the judgment lien is denounced by any provision of the bankruptcy statute. * * * The State court acquired complete jurisdiction and control over the defendants and the property prior to the commencement of the bankruptcy proceeding against Rohrer, and that jurisdiction was not divested by anything done in that proceeding, the rule being applicable that the court which first obtains rightful jurisdiction over the subject-matter should not be interfered with."

But compare, that such suits are stayed ipso facto, *Carpenter Bros. v. O'Connor*, 1 A. B. R. 381, 16 C. C. Ohio 526: "It is not a case in which there is conflict of jurisdiction as between courts of co-ordinate powers where you are called upon to determine which shall have possession of the property. The Court in Bankruptcy has exclusive jurisdiction to take and administer the assets of the bankrupt, pay his debts in so far as the assets will pay them, and discharge him if he is entitled to a discharge from further payment.

"The State court cannot do this. It cannot determine, at the outset, whether or not the defendant is a bankrupt, nor can it discharge him from the further payment of his debts after his property has been exhausted. So that it is a mistaken idea to say that the State court and the Court in Bankruptcy are co-

venency Laws (as was its manifest object), but also for merely foreclosing the mortgage. The court held that the mortgaged property should remain in the hands of the receiver and the trustee be required to intervene and to apply first to the State court. To same effect, analogously, In *re Chapman*, 3 A. B. R. 607, 99 Fed. 395 (D. C. Ga.).

Heller v. LeRoy, 12 A. B. R. 733, 179 N. Y. 369. This was an equitable action instituted to enforce a judgment lien acquired more than four months prior to bankruptcy wherein also fraudulent conveyances interfering with the lien were sought to be set aside. Also, see ante, § 1444.

Contra, In *re Sabine*, 1 A. B. R. 315 (Ref. N. Y.).

Contra, In *re Knight*, 11 A. B. R. 1, 125 Fed. 35 (D. C. Ky.). But in this case the receivership operated more broadly than merely to take custody over the property under the mortgage sought to be foreclosed; it operated also to sequester other property for the benefit of the mortgagee, and to

such extent was voidable under § 67 "f."

Contra, see note to *Taylor v. Taylor*, 4 A. B. R. 211 (N. J. Ch.). In *re Holloway*, 1 A. B. R. 659, 93 Fed. 638 (D. C. Ky.). But in this case the court seems to consider it a matter of discretion.

Compare, analogous propositions ante, §§ 1442, 1444.

Foreclosure Instituted before Four Months.—A fortiori, a foreclosure suit instituted before the four months period would not be superseded; *Sample v. Beasley*, 20 A. B. R. 164, 158 Fed. 666 (C. C. A. La.): *Kneeland v. Pennell*, 18 A. B. R. 538 (City Ct. of N. Y.), wherein the foreclosure of an attorney's lien on a judgment by him for the bankrupt was sustained; nor will the bankruptcy court restrain the foreclosure proceedings. In *re Pennell*, 18 A. B. R. 909, 159 Fed. 500 (D. C. N. Y.). Contra (claiming for the bankruptcy courts "a certain revisory power"), *Hobbs v. Head & Dowd*, 26 A. B. R. 63 (C. C. A. N. H.), discussed in the text of § 1582.

ordinate courts, each having jurisdiction over the subject matter. The State court has nothing to do with the proceedings in bankruptcy.

"The order of procedure in this case should be under the statute as follows: When the petition in bankruptcy was filed by the defendant, all proceedings in the State court should stop. In other words, in the language of the Bankrupt Act as contained in § 11, 'The proceedings shall be stayed.' This is mandatory. The State court has no right to proceed further in an action there pending until the petition in bankruptcy has been adjudicated. When that has been done, the case may be further stated in the State court at its discretion."

The same rule has been held in some cases even where the foreclosure suit is not instituted until *after adjudication* of the mortgagor as bankrupt; ²⁴ and even where not instituted until after discharge.²⁵

Foreclosure by sale, under power of sale, is equally protected with that by suit.²⁶

And the state court's jurisdiction will not be divested even though the lien or transfer therein involved (but not the lien of the suit itself) is claimed by the trustee to be in violation of the bankruptcy provisions relative to voidable preferences.²⁷

And if the suit is a foreclosure suit with incidental prayer appropriate to insolvency proceedings, the state court is not divested of jurisdiction, the prayer for general insolvency relief being disregarded.

Carling v. Seymour Lumber Co., 8 A. B. R. 30, 113 Fed. 483 (C. C. A. Ga.): "The Insolvent Traders' Act, before it was superseded, must have been put in operation at the suit of 'unsecured' creditors. Code Ga. 1895, § 2716; *Cracker Co. v. Brooke*, 91 Ga. 243, 18 S. E. 136. The appointment of a receiver is a jurisdiction often exercised by equity courts in foreclosure suits. The Insolvent Traders' Law provides for a proceeding against insolvents only, and the petition alleges that the defendant therein is insolvent; but that allegation is proper, if not necessary, to obtain a receiver in a foreclosure suit. So of all the averments as to the business embarrassments of the defendant in the petition. They are usual in bills seeking the appointment of a receiver. It is true that the petition contains other averments that are unnecessary and unusual in a foreclosure suit, such as demand and refusal to pay, that the petition is for the benefit of the petitioner and other creditors, etc. These and other averments show that the pleader had in view the Insolvent Traders' Law."

Obiter, Merry v. Jones, 11 A. B. R. 625 (Ga. Sup. Ct.): "Where the main purpose of the suit is to foreclose a mortgage, and there is also an incidental prayer for relief appropriate to insolvency proceedings, a receiver's possession thereunder will not be affected by a subsequent adjudication in bankruptcy."

But if the proceedings are in reality insolvency proceedings with merely incidental prayer for foreclosure, the jurisdiction is divested.

²⁴. In re San Gabriel Sanitorium Co., 7 A. B. R. 206, 111 Fed. 892 (C. C. A. Calif., reversing, on rehearing, its own decision, 4 A. B. R. 197); In re Porter, 6 A. B. R. 259, 109 Fed. 111 (D. C. Ky.); *Heath v. Shaffer*, 2 A. B. R. 98, 93 Fed. 647 (D. C. Iowa); In re Victor Color & Varnish Co., 23 A. B. R. 177, 175 Fed. 1023 (C. C. A. N. Y.).

²⁵. *Evans v. Rounsaville*, 8 A. B. R. 236, 115 Ga. 684.

²⁶. *Harvey v. Smith*, 7 A. B. R. 497 (Sup. Jud. Ct. Mass.).

²⁷. *Furth v. Stahl*, 10 A. B. R. 442, 205 Penn. 439 (Sup. Ct. Penn.); *Savings Bk. v. Jewelry Co.*, 12 A. B. R. 781, 123 Iowa 432.

Merry v. Jones, 11 A. B. R. 625 (Sup. Ct. Ga.): "But where the main purpose of the petition is to obtain relief appropriate only in insolvency proceedings, the fact that a mortgage may be foreclosed as an incident therein will not save the case from the nullifying effect of bankruptcy on pending State insolvency proceedings."

And a suit in equity to enforce any other valid right than a lien will not be interfered with.²⁸

But where a foreclosure suit was started within four months before the bankruptcy but the receiver in the foreclosure suit voluntarily surrendered possession to the trustee in bankruptcy, the bankruptcy court had jurisdiction to marshal liens and to enjoin the further prosecution of the foreclosure suit, though it was not claimed that the liens involved were preferential or otherwise invalid.²⁹ It would seem, however, that jurisdiction was conferred on the bankruptcy court by the surrender of the property by the State court receiver, irrespective of the "four months" apparent qualification of the proposition, it being the actual possession of the res, not the "four months," that conferred the jurisdiction.

§ 1587. Custody of State Court Preserved in Part, and in Part Superseded.—If the suit is a foreclosure suit, or other suit in equity, not creating the lien, but simply enforcing it; but the receiver appointed therein does more than simply conserve the assets subject to the lien, and seizes other assets, although doing so by authority of the State law, the possession of the State Court will be protected as to the assets covered by the lien but will be superseded as to the remainder.³⁰

Carling v. Seymour Lumber Co., 8 A. B. R. 30, 113 Fed. 483 (C. C. A. Ga.): "A receiver or trustee, when appointed in the bankruptcy proceedings, while not entitled to the mortgaged property, will be entitled to any excess arising from the foreclosure sale, when made by order of the State court after the payment of the mortgages and costs of foreclosure. He will also be entitled, when appointed, to the possession of the choses in action and the other property in the hands of the State court's receiver which is not covered by the mortgages. The bankrupt law is equally binding on the State and the Federal court, and we cannot doubt that the former will, on proper application give full effect to it. Where assets are in the hands of the receiver of one court which legally and equitably belong to the trustee or receiver appointed by another court, comity requires, as a general rule, that application should be made for a proper order

28. Compare, analogously, *In re English*, 11 A. B. R. 674, 127 Fed. 940 (C. C. A. N. Y.).

29. *In re Dana*, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.).

30. Obiter, inferentially, *In re Kavanaugh*, 3 A. B. R. 832, 99 Fed. 928 (D. C. Ky.); contra, impliedly, and that it is superseded altogether, see, *In re Knight*, 11 A. B. R. 1, 125 Fed. 35 (D. C. Ky.).

If the lienholder proves his demand in the bankruptcy proceedings, it would

perhaps amount to a waiver of his rights to insist on continuing the foreclosure suit in the State Court. *Reed v. Equitable Trust Co.*, 8 A. B. R. 242, 115 Ga. 780.

But if no seizure nor sequestration of property in the suit in the State Court is made until after the bankruptcy court has assumed jurisdiction the property must be turned over to the bankruptcy court. *Carpenter Bros. v. O'Connor*, 1 A. B. R. 381 (Ohio C. C.). See post, § 1600.

to the former court, whose officer has possession of the property. This rule is reciprocal between the Federal and State courts, each respecting the possession of the other."

Likewise, if the attachment suit operates to do more than enforce a lien obtained before the four months' period, the state court's custody will be superseded as to the remainder.

§ 1588. Attachments Obtained Prior to Four Months, Not Abated.—Where an attachment lien is obtained more than four months prior to bankruptcy, the attaching creditor should be allowed to prosecute his action to judgment and sale, after the bankruptcy.³¹

Likewise, where a garnishment has been effected before the four months.³²

§ 1589. Landlord's Levy.—Seizure, under state statute, by levy of execution by a landlord, upon goods found on the premises, will not be sufficient ground for ordering surrender of the property levied on: the state court will not be superseded.³³

But of course such levy under process of distraint will not be permitted under process from the State court upon property in the custody of the trustee or receiver.³⁴

§ 1590. Partnership Dissolution Suits.—Suits for dissolution of partnership instituted more than four months before bankruptcy will not be disturbed;³⁵ even where the court decrees therein that a previous transfer by the firm of one-half of the firm assets to pay a debt, is valid and free from the claims of the remaining partnership creditors.³⁶

But the state court must not go further and attempt to distribute the surplus among the particular creditors interested in the suit, but must turn it over to the trustee in bankruptcy of the partnership, if the order of distribution is asked for later than four months before the bankruptcy.³⁷

And if they operate to create liens or priority claims different from those prescribed by the Bankruptcy Act itself, and such liens or priorities are created within the four months, then the jurisdiction of the State court may be divested.³⁸

^{31.} In re Snell, 11 A. B. R. 35, 125 Fed. 154 (D. C. Calif.); In re Beaver Coal Co., 7 A. B. R. 542, 113 Fed. 889 (C. C. A. Ore.); Batchelder v. Wedge, 19 A. B. R. 268, 80 Vt. 353; In re Shinn, 25 A. B. R. 833, 185 Fed. 990 (D. C. N. J.). See ante, § 1439, et seq.

^{32.} National Surety Co. v. Medlock, 19 A. B. R. 654, 2 Ga. App. 665, 58 S. E. 1131, quoted at § 1455.

^{33.} In re Seebold, 5 A. B. R. 358, 105 Fed. 910 (C. C. A. La.); Henderson v. Mayer, 28 A. B. R. 387, 225 U. S. 631. See §§ 1437, 1444, 2204.

^{34.} In re Bishop, 18 A. B. R. 635, 153 Fed. 304 (D. C. S. Car.); also, see post, § 1799.

^{35.} In re Price, 1 A. B. R. 606, 92 Fed. 987 (D. C. N. Y.); In re English, 11 A. B. R. 674, 127 Fed. 940 (C. C. A. N. Y.). But compare, contra, if within the four months, Wilson v. Parr, 8 A. B. R. 234, 115 Ga. 629. Compare, Rogers v. Stefani, 19 A. B. R. 566, 156 Fed. 267 (D. C. Ark.).

^{36.} In re English, 11 A. B. R. 674, 127 Fed. 940 (C. C. A., reversing on other grounds, 10 A. B. R. 133).

^{37.} In re English, 11 A. B. R. 674, 127 Fed. 940 (C. C. A. N. Y., reversing 10 A. B. R. 133).

^{38.} Mather v. Coe, 1 A. B. R. 504, 92 Fed. 333 (D. C. Ohio).

§ 1591. Fraudulent Transfer Suits Instituted before Four Months.—Suits to set aside fraudulent transfers instituted more than four months preceding the bankruptcy may not be enjoined, nor may the property be ordered turned over to the trustee in bankruptcy.³⁹

Similarly, fraudulent transfer suits against the bankrupt as transferee, whether instituted before or within the four months, are not superseded by bankruptcy subsequently occurring.

In *re United Wireless Co.*, 27 A. B. R. 1, 192 Fed. 238 (D. C. N. J.) [wherein the court seemed to think it an essential point however, that the suit had been started before the four months period]: "The purpose of that suit is to set aside a certain conveyance of property made by the International Company to the American De Forrest Wireless Telegraph Company, and a conveyance of the same property made by the latter to the United Company, upon the ground that the first conveyance was without consideration and in fraud of the creditors of the International Company, and that the conveyance to the United Company [the bankrupt] was made without consideration and with knowledge on the part of said last named company of the want of consideration and fraud charged concerning the first conveyance. * * * More than four months thereafter the petition in bankruptcy was filed as aforesaid. The suit in the State court is one within its cognizance, and having first obtained such jurisdiction, it should be permitted to finally dispose of it, not only because of the spirit of comity that prevails among courts having concurrent jurisdiction, but also because of necessity, as otherwise the administration of justice would be seriously hampered, if not scandalized, unless by the institution of the bankruptcy proceedings the United States District Court obtained exclusive jurisdiction over the subject matter.

§ 1592. Fraudulent Transfer Suit within Four Months in Aid of Levy Made before Four Months, Not Abated.—And a suit in equity instituted within the four months' period to enforce a judgment lien created before the four months' period will not be superseded because of the creditor's seeking therein to set aside a fraudulent conveyance that interferes with the enforcement of his judgment lien, the lien itself being acquired before the four months and the fraudulent conveyance suit being simply an incident to the enforcement of the lien.⁴⁰

§ 1593. Creditors' Bills Instituted before Four Months.—Creditors' bills instituted more than four months preceding the debtor's bankruptcy are not abated.⁴¹

39. *Pickens v. Dent*, 9 A. B. R. 47, 187 U. S. 177; *Nat'l Bk. of Republic v. Hobbs*, 9 A. B. R. 190, 118 Fed. 626 (U. S. C. C. Ga.); *In re Meyers & Co.*, 1 A. B. R. 347 (Ref. N. Y.); *In re Kavanaugh*, 3 A. B. R. 832, 99 Fed. 928 (D. C. Ky.).

40. *Hiller v. LeRoy*, 12 A. B. R. 733, 179 N. Y. 369.

41. *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165: The Supreme Court held in this case that the plaintiff in a

judgment creditor's action commenced more than four months prior to the filing of the judgment creditor's petition in bankruptcy acquires a lien upon the equitable assets of the bankrupt which is superior to the title of his trustee in bankruptcy thereto.

In re Meyers & Co., 1 A. B. R. 347 (Ref. N. Y.); *Frazier v. Southern Loan & Trust Co.*, 3 A. B. R. 710, 99 Fed. 707 (C. C. A. N. Car., reversing *In re Benbow* (Southern Loan & Trust

§ 1594. Assignments and Receiverships Created before Four Months.—Assignments and receiverships instituted more than four months preceding bankruptcy are not affected.⁴²

In *re Carver & Co.*, 7 A. B. R. 539, 113 Fed. 128 (D. C. N. Car.): "The Act of Congress was not invoked by the filing of a petition in bankruptcy until more than four months after such assignment was made and the estate partly distributed in pursuance thereof. The assignment thus becomes valid and whatever was done under its provisions is also valid."

Obiter, *Rogers v. Stefani*, 19 A. B. R. 566, 156 Fed. 267 (D. C. Ark.): "In this case the said Chancery Court acquired jurisdiction of the persons and property of *Rogers & Stefani*, the bankrupts, more than four months before the proceedings in bankruptcy were begun and if it had retained possession of the property until the order in controversy was made, it would not have lost control of the property, by the adjudication in bankruptcy."

Obiter, In *re Boner*, 22 A. B. R. 151, 169 Fed. 727 (D. C. Va.): "It is to be borne in mind that the bankruptcy law does not undertake to inquire into the assignments and transfers of a man's property made more than four months prior to its proceeding. Nor does it attempt, nor can it attempt, to supervise the course and conduct of insolvency proceedings (here a general assignment) under State law undertaken and carried out more than four months prior to the institution of the bankruptcy proceedings."

§ 1595. Administrators, etc., Where Bankrupt Owns Interest in Estate, Not Disturbed.—Administrators and executors under orders of court in possession of property at the time of bankruptcy, in which the bankrupt has an interest, may not be disturbed.⁴³

§ 1595½. Awards of Arbitrators.—A judgment within the four months period upon an award of arbitrators made before the four months period will not be avoided nor the proceedings thereon be superseded where the lien of such judgment by State law reverts to the date of the award.⁴⁴

Co. v. Benbow), 3 A. B. R. 9, 96 Fed. 514), quoted *supra*; *Nat'l Bk. v. Moses*, 11 A. B. R. 772 (Sup. Ct. N. Y.); In *re Kavanaugh*, 3 A. B. R. 832, 99 Fed. 928 (D. C. Ky.); *Taylor v. Taylor*, 4 A. B. R. 211, 45 Atl. 440 (N. J. Ch.); In *re Heckman*, 15 A. B. R. 500, 140 Fed. 859 (C. C. A. Wash.); inferentially, *Nat'l Bk. of the Republic v. Hobbs*, 9 A. B. R. 190, 118 Fed. 626 (U. S. C. C. Ga.).

⁴² See post, § 1607. In *re Price & Co.*, 1 A. B. R. 606, 92 Fed. 987 (D. C. N. Y.), which was a receivership to wind up a partnership. In *re Kavanaugh*, 3 A. B. R. 832, 99 Fed. 928 (D. C. Ky.); In *re Shinn*, 25 A. B. R. 833, 183 Fed. 990 (D. C. N. J.); In *re Farrell*, 23 A. B. R. 826, 176 Fed. 505 (C. C. A. Ohio), quoted at § 1632.

Inferentially, this proposition is supported by the cases holding that assignments and receiverships created within the four months period are annulled by the bankruptcy, since all such

cases quite invariably insist on the proviso "within four months," see cases cited post, § 1603.

Compare, In *re Sterlingworth Ry. Supply Co.*, 21 A. B. R. 342, 164 Fed. 591, 165 Fed. 267 (D. C. Pa.), where the assets had been in the hands of a State court receiver for more than a year, the court refusing to supersede the State court receiver but not on the ground of its being more than four months.

⁴³ In *re Pierce*, 4 A. B. R. 489, 102 Fed. 977 (D. C. Wash.); compare, *White v. Thompson*, 9 A. B. R. 653, 119 Fed. 868 (C. C. A. Ala.).

Administrator Appointed in One Jurisdiction Not to Be Sued in Representative Capacity in Another.—*Bryan v. Curtis*, 19 A. B. R. 894, affirming 18 A. B. R. 90.

⁴⁴ In *re Koslowski*, 18 A. B. R. 723, 153 Fed. 823 (D. C. Pa.), quoted at § 1459.

§ 1596. Trustee's Intervention in State Court Proceedings Does Not Oust State Court.—The trustee in bankruptcy, by intervening in an action to enforce a specific lien upon an insolvent's assets, in a State Court, does not thereby oust the State Court of jurisdiction.⁴⁵

§ 1597. State Courts Administer Bankrupt Law and Trustee, Intervening, Not Confined to Rights Accorded by State Law.—The Bankrupt Act is equally binding on State and Federal Courts, and where the trustee has intervened in a State Court proceeding, he is not confined to the rights accorded by State law in the absence of bankruptcy but may urge rights and defenses given by the Bankrupt Act; it being simply as to the forum and not as to the rights that he is relegated to the State court.⁴⁶

Carling v. Seymour Lbr. Co., 8 A. B. R. 41, 113 Fed. 483 (C. C. A. Ga.): "The laws of the United States being equally binding on all the courts, we cannot assume that the State court would refuse to administer them. We are not now called on to decide what course should be taken in the event of a disregard of the Bankrupt Law by the State court."

Obiter, *In re Dana*, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.): "A considerate regard for the dignity of the courts of the States, so essential to harmony in our intricate judicial systems, forbids an assumption that they will not be equally solicitous to observe the Constitution and laws of the United States, which constitute the supreme law of the land binding upon all the courts."

§ 1598. Bankruptcy Court May Enjoin to Permit Intervening of Trustee.—But the bankruptcy court may restrain the state court long enough to enable a trustee to be elected, and for him to intervene to protect the creditors' rights.⁴⁷

DIVISION 1.

FIRST EXCEPTION TO RULE THAT STATE COURT RETAINS JURISDICTION IF FIRST TO OBTAIN IT: NULLIFIED LEGAL LIENS.

§ 1599. First Exception to Rule That State Court Retains Jurisdiction if First Obtaining Possession.—To the rule that the State Court

45. *Des Moines Bk. v. Morgan Jewelry Co.*, 12 A. B. R. 781, 123 Iowa 432.

Profits on Operation of Oil Well by Trustee Who Takes Possession Notwithstanding State Court's Prior Custody.—Compare peculiar situation in *In re St. Louis & Kansas Coal Co.*, 22 A. B. R. 56, 168 Fed. 934 (D. C. Kans.), where the trustee intervened in pending suits wherein injunction had been issued, etc., and, apparently without protest from State court, operated oil wells in controversy, the question then arising as to whom the profits should be decreed.

46. *Heath v. Schaffer*, 2 A. B. R. 102, 93 Fed. 647 (D. C. Iowa). See post, § 1687. *Des Moines Bk. v. Morgan Jewelry Co.*, 12 A. B. R. 781, 123 Iowa 43,

quoted supra, § 1582; *Obiter*, *Hurley v. Devlin*, 18 A. B. R. 627, 151 Fed. 919 (D. C. Kan.); *obiter*, *In re Tracy & Co.*, 23 A. B. R. 438, 177 Fed. 532 (D. C. N. Y.); *In re Martin*, 27 A. B. R. 545, 193 Fed. 841 (C. C. A. Ky.); *Hall v. Chicago, etc., R. Co.*, 25 A. B. R. 53 (Sup. Ct. Neb.).

47. See post, § 1901; also see *In re Klein*, 3 A. B. R. 174, 97 Fed. 31 (D. C. Ills.); *In re Donnelly*, 26 A. B. R. 304, 188 Fed. 1001 (D. C. Ohio). *Obiter*, *Carling v. Seymour Lumber Co.*, 8 A. B. R. 41, 113 Fed. 438 (C. C. A. Ga.). Compare remarks of court as to "a certain revisory power" in *Hobbs v. Head & Dowst Co.*, 26 A. B. R. 63, 185 Fed. 1006 (C. C. A. N. H.).

will retain jurisdiction if it is the first to obtain custody of the property, there are three exceptions: First, where the possession of the State Court has itself created a lien by legal proceedings within four months of the bankruptcy, whilst the debtor was insolvent; second, where a receiver, assignee or trustee appointed by the State Court within four months of the bankruptcy, is in possession; third, where the possession is under State Insolvency proceedings that are superseded by the Bankrupt Act.

First exception: Where the possession of the state court has created a lien by legal proceedings within four months of the bankruptcy and while the debtor is insolvent, the State Court does not retain jurisdiction; but the property affected must, upon adjudication of bankruptcy, be surrendered to the bankruptcy court.⁴⁸

This is so for the reason that the *lien* thus created is itself null and void, and being created by the legal proceedings the legal proceedings themselves are null and void and fall to the ground. This exception, then, does no real violence to the principle that the court first obtaining jurisdiction of the res retains jurisdiction.

§ 1600. Same Subject Discussed, Ante, "Liens by Legal Proceedings Nullified by Bankruptcy."—The nature of § 67 "f" nullifying such liens, and the elements that must be in attendance in order that the lien be nullified, and the limitations of the rule, are fully expounded ante, under the subject of "Liens by Legal Proceedings Nullified by Bankruptcy;" as are also the general rules as to procedure in obtaining surrender of such property to the trustee.⁴⁹

Thus, if a creditor has attached property of an insolvent debtor and, within four months thereafter, a bankruptcy petition is filed by or against the debtor and the debtor is eventually adjudged bankrupt, the attachment proceedings, as already noted, are nullified, and the sheriff or constable may be required to surrender possession of the property; although, of course, nothing prevents the suit from continuing to its finish to a judgment in personam against the debtor, if the debtor himself does not stay it. But as to the property, the bankruptcy court seizes possession of it, and wholly supersedes the state court in its administration.⁵⁰

It is to be borne in mind, also, that the bankruptcy must have occurred within four months of the levying of the attachment or other creation of the legal lien, else the legal proceedings are not made null nor void;⁵¹ and the only thing the trustee can do in case the bankruptcy comes later than four months thereafter, is to get admitted to the proceedings in the State court,

⁴⁸. In re Martin, 27 A. B. R. 545, 193 Fed. 841 (C. C. A. Ky.); Instance, In re Oxley & White, 25 A. B. R. 656, 182 Fed. 1019 (D. C. Wash.).

⁴⁹. Ante, § 1429. See also, subject of "Summary Orders on Custodians and

Court Officers in Possession," post, § 1830.

⁵⁰. See ante, §§ 1448, 1449. In re Ransford, 28 A. B. R. 78, 194 Fed. 658 (C. C. A. Mich.).

⁵¹. See ante, § 1439.

as a party, and to litigate his rights there, being content with whatever the State court may say is his rightful share of the proceeds.

Thus, also, where the suit is in part a mere foreclosure suit or other suit to realize upon a valid pre-existing lien and in part creates a lien by legal proceedings upon other assets of the insolvent during the four months' period, the jurisdiction of the State Court will be protected as to the first part and be superseded as to the latter part.⁵²

Thus, also, until the adjudication in bankruptcy takes place the legal proceedings are not superseded and a court office in possession of assets may not be proceeded against summarily. It may occur that the lien may never be rendered void.⁵³

But when the adjudication does take place, the nullity and invalidity relate back to the date of the levy or seizure by legal proceedings, and the State Court is superseded.⁵⁴

§ 1601. When Lien Nullified Property Recoverable by Summary Order.—When the lien is nullified the property affected by it is recoverable by summary order.⁵⁵

DIVISION 2.

SECOND EXCEPTION GENERAL ASSIGNMENTS, RECEIVERSHIPS ETC., NULLIFIED BY BANKRUPTCY.

§ 1602. Second Exception to Rule That State Court Retains Jurisdiction if First Obtaining Custody.—The second exception to the rule that the State Court retains jurisdiction if it first obtains the custody of the property involved is **where the property at the time of the Bankruptcy is in the possession of an assignee for the benefit of creditors or of a receiver or trustee appointed outside of bankruptcy, where the assignment, receivership or trusteeship is created within the four months preceding the filing of the bankruptcy petition, in which event upon the adjudication in bankruptcy occurring, the Bankruptcy Court supersedes the insolvency court and the court**

52. See ante, § 1587.

For a case where the court refused to enjoin execution sale, where levy was made within four months on judgment obtained several years beforehand, relegating the parties to the State Court for action on the ground of comity, see *In re Shoemaker*, 7 A. B. R. 437, 112 Fed. 648 (D. C. Va.).

For a case where the Circuit Court of Appeals reversed the District Court and refused to stay an attachment case and relegated the parties to the State court on the ground of prior possession of the res, see *Marble Co. v.*

Grant, 14 A. B. R. 288, 135 Fed. 322 (C. C. A. Penn.).

But attachment suits in Pennsylvania, it is understood, may be used to assert title or ownership in the res; in such cases such ruling would not be contrary to the main proposition.

53. See post, § 1609; "Summary Orders on Court Officers," § 1828.

54. See ante, § 1467.

55. Apparently, *In re McCartney*, 6 A. B. R. 368, 109 Fed. 629 (D. C. Wis.).

See ante, § 1471, et seq; post, "Summary Orders on Custodians and Court Officers," § 1830, et seq.

appointing the assignee, receiver or trustee and takes over the property involved for administration in Bankruptcy.⁵⁶

Randolph v. Scruggs, 10 A. B. R. 1, 190 U. S. 533: "It is admitted that a general assignment for the benefit of creditors made within four months from the filing of a petition in bankruptcy, is void as against a trustee in bankruptcy, so far as it interferes with his administering the property assigned. This could not be denied."

§ 1603. Basis of Superseding Custody of Assignee and Receiver.

—The rule that the bankruptcy court supersedes the custody of the State court in cases of assignments, receiverships, etc., created within the four months period, is said to have for its basis the necessary implication arising from such assignments and receiverships being specifically declared to be acts of bankruptcy. Since they operate—if allowed to stand—to take away the very fruits of the adjudication itself and to render the adjudication purposeless, the necessary implication arises, it is said, that the assignments and receiverships themselves become void.⁵⁷

56. *Cohen v. American Surety Co.*, 20 A. B. R. 65 (Court of Appeals of N. Y.); *In re Cameron Currie & Co.*, 20 A. B. R. 790 (Ref. Mich.).

Compare, "General Assignments, Receiverships and Trusteeships as Acts of Bankruptcy," ante, § 144, et seq. Compare, "General Assignments and Receiverships Held to Amount to State Insolvency Laws," post, § 1634, division 3, this chapter.

The following cases were receivership and assignment cases, to be sure, but were held in many instances to amount to State Bankruptcy or State Insolvency proceedings, hence in many of these cases the superseding of the State Court's custody is to be based on entirely different principles, the principles discussed in division 3 of chapter XXXII:

In re Storck Lumber Co., 8 A. B. R. 86, 114 Fed. 860 (D. C. Md.); *In re Lengert Wagon Co.*, 6 A. B. R. 536, 110 Fed. 927 (D. C. N. Y.); *obiter*, *In re Kersten*, 6 A. B. R. 516, 110 Fed. 929 (D. C. Wis.); *Mauran v. Carpet Lining Co.*, 6 A. B. R. 734 (Sup. Ct. R. I.).

Compare, as being act of Bankruptcy, *In re Milbury Co.*, 11 A. B. R. 523 (D. C. N. Y.). Compare, apparently to same effect, *In re Watts*, 10 A. B. R. 113, 190 U. S. 1; *In re Smith & Dodson*, 2 A. B. R. 9 (D. C. Ind.); apparent instance, *In re Etheridge Furn. Co.*, 1 A. B. R. 115, 92 Fed. 329 (D. C. Ky.); apparent instance, *In re McKee*, 1 A. B. R. 311 (Jefferson County Ct. Ky.); *In re Curtis*, 1 A. B. R. 440, 91 Fed. 737 (D. C. Ills.), which was an assignment case. *In re Gutwillig*, 1 A. B. R. 388,

92 Fed. 337 (C. C. A. N. Y., affirming 1 A. B. R. 78, reasoning approved in *Lea v. West*, 174 U. S. 590, 2 A. B. R. 463); *David v. Bohle*, 1 A. B. R. 412, 92 Fed. 325 (C. C. A. Mo., affirming *In re Sievers*, 1 A. B. R. 117); *In re Sievers*, 1 A. B. R. 117, 91 Fed. 366 (D. C. N. Y.), affirmed sub nom. *Davis v. Bohle*, 1 A. B. R. 412, 92 Fed. 325 (C. C. A. Mo.); *In re Gray*, 3 A. B. R. 647 (N. Y. Sup. Ct.); impliedly, *In re Thompson*, 11 A. B. R. 720, 128 Fed. 575 (C. C. A. N. Y.); *In re Knight*, 11 A. B. R. 1, 135 Fed. 25 (D. C. Ky.); *In re Watts*, 10 A. B. R. 113, 190 U. S. 1.

In re Brown, 1 A. B. R. 110, 91 Fed. 358 (D. C. Ore.): "Nor can the fact that the property is in the hands of a receiver, in a suit to set aside an alleged fraudulent conveyance, affect the question. The immunity which the prior conveyance has, under the Bankrupt Act, does not extend to the legal custody taken in a suit to cancel the conveyance, the property having in the meantime been voluntarily restored by the fraudulent grantee to the bankrupt."

Obiter, *In re Hirose*, 12 A. B. R. 154 (D. C. Hawaii); inferentially and *obiter*, *In re Romanow*, 1 A. B. R. 461, 92 Fed. 510 (D. C. Mass.); *In re Fellerath*, 2 A. B. R. 40, 95 Fed. 121 (D. C. Ohio); *obiter*, *Leidigh Carriage Co. v. Stengel*, 2 A. B. R. 383, 95 Fed. 637 (C. C. A. Ohio); *In re Etheridge Furn. Co.*, 1 A. B. R. 115, 92 Fed. 329 (D. C. Ky.).

57. *Cohen v. American Surety Co.*, 22 A. B. R. 909, 132 App. Div. (N. Y.) 917, dissenting opinion.

Obiter, Randolph v. Scruggs, 190 U. S. 533, 10 A. B. R. 3: "It is admitted that a general assignment for the benefit of creditors, made within four months from the filing of a petition in bankruptcy, is void as against a trustee in bankruptcy, so far as it interferes with his administering the property assigned. This could not be denied. *West Co. v. Lea Bros.*, 174 U. S. 590, 595, 2 Am. B. R. 463, 43 L. Ed. 1098, 1099; *Boese v. King*, 108 U. S. 379, 385, 27 L. Ed. 760, 762; *Bryan v. Bernheimer*, 181 U. S. 188, 5 Am. B. R. 623, 45 L. Ed. 814. It hardly is necessary to discuss whether such an assignment should be held to be embraced in the express avoidance of conveyances made with intent to hinder, delay, or defraud creditors in § 67e of the Bankruptcy Law. * * * It is possible to say that constructively a general assignment falls under that description. * * * One ground for such a construction would be that making the assignment is declared an act of bankruptcy by § 3. As it could not have been intended that the very conveyance which warranted putting the grantor into bankruptcy should withdraw all his property from distribution there, it seems sufficient to rely upon the necessarily implied effect of § 3. * * * If by declaring the assignment an act of bankruptcy, the statute means that the conveyance shall not be effectual against the bankruptcy proceedings, as is agreed, the natural and simple construction is that it means that the deed shall be avoided as a whole when the trustee takes the goods."

In *re Knight*, 11 A. B. R. 6, 125 Fed. 35 (D. C. Ky.): "* * * it is the established doctrine in bankruptcy that an assignee, under a deed of general assignment, and the execution of which deed is the act of bankruptcy upon which the adjudication is made, although he has qualified in the County Court and is acting under its orders, does not hold the estate of the bankrupt adversely to the trustee in bankruptcy. It thence logically and necessarily follows that the assignee holds the property subject to the right of the requisite number of creditors having debts amounting in the aggregate to the sum of \$500 to avail themselves of the act of bankruptcy and secure an adjudication, and that when this is done the rights of the creditors relate back to the act of bankruptcy, and override all intermediate or intervening attempts by the assignee to overreach or defeat the results of the act of bankruptcy, or the rights of creditors arising out of it. The general principle which underlies the subject, and which cannot be ignored, must be this: When a general assignment for the benefit of creditors is made by a debtor, eo instanti there is generated by the statute a right in his creditors to have his affairs wound up and his estate administered in the bankruptcy court pursuant to the Bankrupt Law, which has suspended the operation of all State insolvency laws; and, if the enforcement of this right is demanded by a proper proceeding within four months after its inception, no action in any court in any suit brought after the commission of the act of bankruptcy can defeat it without the consent of the bankrupt court. Quoad hoc, the jurisdiction of the bankruptcy court is necessarily exclusive and supreme. * * * In other words, the rights of creditors, inchoate from the making of the assignment, ripen into maturity when the adjudication is made. If it were otherwise the Bankruptcy Law could be evaded with the utmost facility."

Davis v. Bohle, 1 A. B. R. 412, 92 Fed. 325 (C. C. A. Mo.): "This (§ 3, making assignments acts of bankruptcy) was but another form of saying that if a person, subject to the provisions of the act, should make a general assignment, it should entitle his creditors to have him adjudged a bankrupt within four months after the commission of the act, and to have his estate administered by a trustee or trustees of their own selection, pursuant to the provisions of the act, rather than by the assignee who had been chosen by the insolvent debtor for that purpose. Inasmuch as an assignee under a voluntary

deed of assignment is not a purchaser for value of the assigned property, but is merely an agent or trustee of the assignor and his creditors, and holds the assigned property solely for their benefit, Congress, when it provided that a general assignment should be regarded as an act of bankruptcy, did not deem it necessary to say further, and in so many words, that the assigned property might be taken from the custody of the assignee at the instance of creditors, if the assignor was subsequently adjudged a bankrupt. It was assumed, no doubt, that by declaring a general assignment to be an act of bankruptcy, with all which that declaration implied, the assignee named in such a deed would take a defeasible title to the assigned property, which would instantly fail when the assignor was adjudged a bankrupt, and that he would thenceforth be accountable to the trustee appointed in bankruptcy proceedings for the assigned property or its proceeds. Such, we think, is the necessary effect of the clause making a general assignment an act of bankruptcy, when that clause is read in the light of decisions both in this country and England construing prior bankrupt laws, which decisions must be presumed to have been well known to the lawmaker. Thus, under an English bankrupt act (6 Geo. IV. ch. 16, § 3), which made it an act of bankruptcy if a person executed any fraudulent conveyance or transfer with intent to defeat or delay his creditors, it was repeatedly held that a voluntary assignment by a debtor of his whole estate for the equal benefit of all his creditors was an act of bankruptcy, within the meaning of the aforesaid statute, not because such a conveyance was fraudulent in fact, but because it was constructively fraudulent, and in violation of the Bankrupt Act, in that it provided for a different mode of administration upon the effects of the insolvent debtor than that contemplated by the act."

Hooks v. Aldridge, 16 A. B. R. 664, 145 Fed. 865 (C. C. A. Tex.): "We have before us a record showing that a State court, because of insolvency, appointed a receiver for a corporation and placed him in possession of its property, and that thereupon, and on that ground, among others, the court of bankruptcy adjudged the corporation a bankrupt, pursuant to the amendment we have quoted. In enacting these additional grounds of involuntary bankruptcy, it could not have been the intention of Congress that the receiver of the State court appointed 'because of the insolvency' of the corporation, should continue to hold possession of the property and to administer and settle the estate. The Supreme Court observed in a recent case that 'the operation of the bankruptcy laws of the United States cannot be defeated by insolvent corporations applying to be wound up under State statutes' (*In re Watts & Sachs*, 190 U. S. 1, 27, 10 Am. B. R. 113, 23 Sup. Ct. 718, 47 L. Ed. 933): nor can they be defeated by the appointment of receivers, because of insolvency, at the suits of their officers, stockholders, or creditors."

The obvious weakness of such reasoning would seem to be that the right to supersede the State court's custody would logically apply only where such general assignment or receivership is the very ground of the adjudication in bankruptcy itself, thus leaving assets to continue in the control of the State Court receiver or assignee where the adjudication is based on other grounds or is on voluntary petition. One court, in evident anticipation of such argument, in a case where a general assignment was first made and afterwards a receiver was appointed in a mortgage foreclosure suit to collect the rents of the mortgaged property in behalf of the mortgagee, held that, although the assignment was the act of bankruptcy upon which the ad-

judication was obtained, nevertheless not only was the assignment itself nullified but also all subsequent dispositions of the property.

In *re Knight*, 11 A. B. R. 1, 125 Fed. 35 (D. C. Ky.): “* * * can the rights of the creditors to have the bankrupt’s estate administered in the bankruptcy court, and under the Bankruptcy Law be defeated by the expedient of thereafter hurriedly bringing suit in the State court, in which, upon an allegation of insolvency, a receiver is appointed and put in charge of the debtor’s property—things which, of themselves, under the amendment of 1903, * * * constituted a further act of bankruptcy, upon which alone an adjudication could have been secured? And just at this point we may well inquire whether, if an adjudication in bankruptcy had been made upon a creditor’s petition alleging, in the language of the amendment of February 5, 1903, that because of insolvency a receiver had been put in charge of Knight’s property by the State court, that court, under the doctrine and rule of comity, and the supposed teachings of the case of *Peck v. Jenness*, would be still entitled to administer the assets, notwithstanding the Bankruptcy Law. This inquiry would seem to reach the kernel of the matter, for if a State Court could thus do the very thing which constitutes an act of bankruptcy, and at the same time defeat it on the doctrine of comity and priority of jurisdiction, the new ground of bankruptcy is a manifest delusion. These suggestions seem to me to show that the expedient resorted to in this case, under the facts and circumstances surrounding it, cannot defeat the rights of the general creditors, which related back to the doing of the thing upon which the adjudication in bankruptcy was made.”

But this counter argument only partly avoids the weakness adverted to. What would become of the prior assignment had not it, but rather the subsequent receivership, been the ground of the adjudication, both being within the four months period?

More naturally, one would expect to find the basis of the superseding of the state courts in some express provision of the statute concerned in *pari materia* with the subject of the right of the trustee to recover assets from third parties, such as are §§ 67, 70, etc., rather than in § 3, relating merely to the determination of the status of the debtor as a bankrupt. Moreover, § 3, relating solely to what acts warrant adjudication of bankruptcy, equally as well makes a preferential transfer an act of bankruptcy, yet Congress did not leave the avoidance of preferences to mere “necessary implication” from that section of the statute, but provided specifically therefor in § 60. The question naturally arises then why Congress should have left the superseding of the custody of the state court in the important cases of assignments, receiverships, etc., to mere implication from the provisions of another section of the act and yet deem it necessary elsewhere to make specific provisions as to the recovery of preferences, although preferences are likewise referred to in that same section as acts of bankruptcy.

It has also been held that the basis is that such assignments and receiverships are transfers made to hinder, delay and defraud creditors under § 67 (e).⁵⁸

⁵⁸ In *re Gray*, 3 A. B. R. 647 (N. Y. Sup. Ct.); inferentially, *Randolph v. Scruggs*, 10 A. B. R. 3, 190 U. S. 533; *obiter*, *Chem. Nat’l Bk. v. Meyer &*

In *re Knight*, 11 A. B. R. 1, 135 Fed. 25 (D. C. Ky.): "Besides, it is important to remember that, whether so in fact or not, a deed of general assignment is constructively fraudulent, and, in legal contemplation, its purpose is to hinder and delay creditors, within the meaning of § 67e of the Statute of 1898 (30 Stat. 564), and consequently that under that section the assigned property, if the deed was made within four months before the filing of the petition in bankruptcy, belongs to the trustee, and by the express terms of the section it is made his duty to recover and reclaim it."

West Co. v. Lea, 174 U. S. 590, 2 A. B. R. 467: "Such consequences was held to arise, from a deed of that description, as a legal result of the clause, in the Act of 1867, forbidding assignments with 'intent to delay, defraud, or hinder' creditors, and from the provision avoiding certain acts done to delay, defeat, or hinder the execution of the act."

It would seem to be improper, however, to classify such resorting to the duly constituted courts of the State among the fraudulent transfers reprobated by § 67 (e), unless an actual fraudulent intent existed.

Ketcham v. McNamara, 6 A. B. R. 162, 72 Conn. 709: "The present bankruptcy law differs from that of 1867 in its mode of treating assignments for the benefit of creditors made without preferences prior to the institution of bankruptcy proceedings. The Act of 1898 declares every assignment of that kind an act of bankruptcy. * * * Under that of 1867 (§§ 26, 86, as amended in 1868 [15 Stat. at L. 228]), it was such only if made in fraud of creditors, and the assignee in bankruptcy could not recover the property without proof that the person receiving it 'had reasonable cause to believe that a fraud on this act was intended.' While the law stood thus, we therefore held that an honest conveyance by an insolvent debtor under our insolvent laws, without actual fraud, and with no actual intent to defeat the operation of the Act of Congress, could not be treated as absolutely void. *Hawkin's Appeal*, 34 Conn. 548, 551. The claim that it was such was set up in that case by one of the general creditors, but apparently only because, if sustained, it would prevent the assignment from operating as a dissolution of an attachment which he had previously made, and thus work a preference in his favor. Such a result the court was indisposed to promote by a construction of the bankruptcy law which would frustrate its main purpose. *Reed v. McIntyre*, 98 U. S. 507, 513.

"The Supreme Court of the United States, in another case, where the equities were of a similar character, held that if the Act of 1867 ipso facto suspended the operation of the insolvent laws of the States, general assignments under those laws, not followed by bankruptcy proceedings, when made with no actual intent to defraud, were not so absolutely void that a judgment creditor of an assignor could hold the assignee to account for the proceeds of the property. *Boese v. King*, 108 U. S. 379, 385, affirming 78 N. Y. 471."

And in still other cases it has apparently been held that the basis is to be found in the principle that the Bankruptcy Law is paramount in the administration of insolvent estates, and that the custody of another court is inconsistent therewith and hence superseded.⁵⁹

Dickinson, 1 A. B. R. 570 (D. C. N. Y.); In *re Slomka*, 9 A. B. R. 637, 122 Fed. 630 (C. C. A. N. Y.). Compare, analogously (Act of Bankruptcy), *Rumsey v. Machine Co.*, 3 A. B. R. 704, 99 Fed. 699 (D. C. Mo.). Compare,

analogously (Act of Bankruptcy), *Salmon v. Salmon*, 16 A. B. R. 122, 143 Fed. 395 (D. C. Mo.).

⁵⁹ Obiter, *Scheuer v. Book Co.*, 7 A. B. R. 390, 112 Fed. 407 (C. C. A. Ala.); obiter, *Leidigh Carriage Co. v.*

In *re Watts*, 190 U. S. 1, 10 A. B. R. 113: "And the operation of the bankruptcy laws of the United States cannot be defeated by insolvent commercial corporations applying to be wound up under State statutes. The Bankruptcy Law is paramount, and the jurisdiction of the Federal courts in bankruptcy, when properly invoked, in the administration of the affairs of insolvent persons and corporations, is essentially exclusive. Necessarily when like proceedings in the State courts are determined by the commencement of proceedings in bankruptcy, care has to be taken to avoid collision in respect of property in possession of the State courts. Such cases are not cases of adverse possession or of possession in enforcement of pre-existing liens, or in aid of the bankruptcy proceedings. The general rule as between courts of concurrent jurisdiction is that property already in possession of the receiver of one court cannot rightfully be taken from him without the court's consent, by the receiver of another court appointed in a subsequent suit, but that rule can have only a qualified application where winding up proceedings are superseded by those in bankruptcy as to which the jurisdiction is not concurrent. Still it obtains as a rule of comity, and accordingly the receiver of the District Court brought his appointment to the knowledge of the Floyd Circuit Court and requested the delivery of the assets."

In *re Curtis*, 1 A. B. R. 444, 91 Fed. 737 (D. C. Ill.): "The object of enumerating in the National Bankruptcy Act what shall constitute an act of bankruptcy is for the very purpose of specifying with certainty what estates shall be administered in the Bankrupt Court. And, in declaring that whosoever should attempt to distribute his estate by a general assignment should be adjudged a bankrupt, it is also the plain intent of the law that such person should not be permitted, after the first day of July, 1898, to do so, but, instead, such estate must be administered in the precise manner pointed out by the National Bankrupt Act.

"From this it is obvious that not only the main object of the State and Federal laws are identical, but also that they both expressly provide a manner of administering the estate of whosoever shall make a general assignment. This being the case, one must yield to the other. One must be operative, and the other inoperative. Both cannot be in full force and effect at the same time. Which remains paramount and operative cannot be in doubt. That the State law shall be suspended is now well settled, and it is therefore the opinion of this court that the proceedings under the general assignment made by the Bank of Waverly, and in the Morgan County Court, are wholly unauthorized and void."

But the reasoning of such rule would apply equally to all cases of insolvency, regardless of the four months' limitation. In reality, such reasoning can only be applicable to cases where the legal proceedings amount to State bankruptcy or State insolvency proceedings, which themselves are superseded in toto, and would come rather under the next division, which discusses the third exception to the main rule. It would hardly apply to mere general assignments and receiverships, except perhaps when they amount, in effect, to State bankruptcy or State insolvency proceedings.

Perhaps, on ultimate analysis, this basis is more properly reducible to the fact that such assignments and receiverships operate to create liens by

Stengel, 2 A. B. R. 383, 95 Fed. 637 (C. C. A. Ohio); In *re Etheridge Furn. Co.*, 1 A. B. R. 115, 92 Fed. 329 (D. C. Ky.);

In *re McKee*, 1 A. B. R. 311 (Jefferson County Ct. Ky.); In *re Fellerath*, 2 A. B. R. 40, 95 Fed. 121 (D. C. Ohio).

legal proceedings in behalf of creditors and thus are made null and void by § 67 (c) and (f), if created within the four months period. Although such liens redound to the benefit of all creditors and not simply to a part, they are nevertheless liens by legal proceedings, quite as much as those created by creditors' bills or suits, brought in behalf of all creditors to set aside fraudulent conveyances, which are held to be clearly within § 67.⁶⁰

Mauran v. Carpet Lining Co., 6 A. B. R. 739, 50 Atl. 331, 387 (Sup. Ct. R. I.): "The United States Bankruptcy Act, § 67, clause 'f,' contains this provision [quoting § 67 'f']:

"It seems to us that the word 'judgment,' as used above, is sufficiently broad to apply to the judgment of this court in appointing the receiver of the Crown Carpet Lining Co., and that the adjudication of bankruptcy against said corporation nullified and avoided the judgment of this court, and that the property held by the receiver must be turned over for administration under the bankruptcy proceedings."

The case *In re Farrell*, 23 A. B. R. 826, 176 Fed. 505 (C. C. A. Ohio), quoted at § 1632, although reaffirming the doctrine of *Mayer v. Hellman*, 91 U. S. 496, and holding that the general assignment must be within the four months of bankruptcy else it will be valid, does not aid us in ascertaining the basis of the superseding of the custody of the assignee in such a case. The case *In re Farrell* seems to assume that Congress has expressly fixed a limit of four months for the avoidance of assignments, but Congress has done no such thing in express terms, and it is only by construction that the qualification of four months limit is to be made.

Impliedly, *In re Fish Bros. Wagon Co.*, 21 A. B. R. 149, 164 Fed. 553 (C. C. A. Kans.): "We think that a title or lien acquired by an assignee under a general assignment valid according to the laws of the State where it is made, that is to the advantage of the estate when it has passed into bankruptcy, is not necessarily destroyed by the supersession of the assignment proceeding, but that upon the order of the court of bankruptcy it may be retained by the trustee for the benefit of the creditors. This conclusion is in harmony with the object sought by express provisions of the Bankruptcy Act for the preservation of liens obtained in judicial proceedings against the debtor. * * * Attention therefore turns to the effect of the general assignment and the provisions of § 67. * * * The general doctrine is that an assignee in a general assignment under a State statute is neither an innocent purchaser nor a creditor having a lien on the assigned property, but that, like a trustee in bankruptcy, he stands in the shoes of his insolvent and is possessed of no greater right. It seems, however, to be otherwise in Kansas. In *Withrow v. Citizens' Bank*, 55 Kan. 378, 40 Pac. 639, it was held that an assignee is not merely the representative of the debtor but is also a trustee for the creditors, in whom title is vested by the deed of assignment, and that an unfiled chattel mortgage is void as against the right so secured by him. The effect of the assignment in question here is to be determined by the Kansas law (*First Nat. Bank v. Staake*, 202 U. S. 141, 15 Am. B. R. 639, * * *) and it is the same upon an unfiled contract of conditional sale as upon an unfiled chattel mortgage. So, had no bankruptcy proceeding been

60. *Wilson v. Parr*, 8 A. B. R. 234 (D. C. Ga.). Likewise see same underlying principle adverted to, although not distinctly announced, in *Davis v. Bohle*, 1 A. B. R. 412, 92 Fed. 325 (C. C. A. Mo., affirming *In re Sievers*, 1 A.

B. R. 117). See interesting though sarcastic discussion, obiter, in *Singer v. Nat'l Bedstead Co.*, 11 A. B. R. 287 (Ct. Chancery N. J.). Compare, *Trust Co. v. Savings Bk.*, 27 A. B. R. 821 (C. C. A. Mich.).

instituted, the assignee would have prevailed over the wagon company in a contest for the possession of the property. Is the right of the assignee available to the trustee, or was it wholly destroyed by the bankruptcy proceeding? The trustee relies upon subdivisions 'a,' 'c,' and 'f' of § 67 of the Bankruptcy Act. The last of these authorizes the preservation, for the benefit of the bankrupt estate, of liens obtained, through legal proceedings against the insolvent debtor within four months prior to the filing of a petition in bankruptcy against him, and subdivision 'c' provides for the subrogation under certain conditions of the trustee to the rights of one who acquires a lien by a suit or proceeding at law or in equity begun against the debtor within the four months' period. There is difficulty in the application of these provisions to the case at bar. Although the right of the assignee under the assignment might be called a 'lien' in the sense that it is a right to resort to specific property for the satisfaction of the debts of the assignor, and is therefore a charge upon such property, and while the assignment proceeding considered in its entirety may be termed a 'legal proceeding,' because under the Kansas law it is conducted in a court of record, yet it is a voluntary proceeding, and is not, as contemplated by the provisions of the Bankruptcy Act above referred to, a proceeding against the insolvent debtor. We think, however, that § 67a is sufficiently comprehensive to cover the case. It provides: 'Claims which for want of record or for other reasons would not have been valid liens as against the claims of the creditors of the bankrupt shall not be liens against his estate.' At the time of the institution of the bankruptcy proceeding the creditors, through the assignee as their representative, had obtained by the general assignment, which was entirely valid under the local law, a right to have the property now in controversy subjected to the payment of their debts, to the exclusion of the claim of the wagon company under its unfiled contract of conditional sale. Because the assignment was superseded by the bankruptcy proceeding, it does not follow that no rights whatever could grow out of it. True, the making of the assignment was an act of bankruptcy; but, when made, it was authorized by the law of the State, and was valid until done away with by a proceeding that took precedence. An assignment cannot be said to be absolutely prohibited by the Bankruptcy Act, irrespective of the institution of a bankruptcy proceeding. *Randolph v. Scruggs*, 190 U. S. 533, 537, 10 Am. B. R. 1. Though the title of a trustee in bankruptcy to the property he takes is not by way of succession to that of an assignee under an assignment that is superseded, yet in such cases many things done by the latter for the benefit of the estate may be retained and enjoyed by the former. As already observed, the assignee, as the representative of all the creditors, had secured a specific right in the property in controversy by a deed of assignment valid under the Kansas law; and if this right, beneficial, as it is, to the bankrupt estate, is to be stricken down, it must be because the assignment was wholly invalid for every purpose and the invalidity related back to the date of the deed. That might be so in case of actual fraud, but there was no such element in the particular transaction."

Inferentially, *In re Gutwillig*, 1 A. B. R. 388, 92 Fed. 337 (C. C. A. N. Y., affirming 1 A. B. R. 78): "These provisions of (§§ 67 'c' and 67 'f') manifest unmistakably the intention of Congress, not only not to permit preferences to be acquired upon the bankruptcy of a debtor when he is about to become a bankrupt, but also to annul all dispositions of his property, except to innocent purchasers, which will defeat the rights of creditors to a distribution by the instrumentalities and according to the schemes of the Bankrupt Act."

And possibly the nullification would come about rather from the provisions of § 67 "c," than from those of § 67 "f," for proof of insolvency is essential under § 67 "f," but is not essential under § 67 "c," where the lien by legal proceedings within the four months period was "sought and permitted in fraud of the provisions of the act."⁶¹

Compare reasoning *West Co. v. Lea*, 174 U. S. 590, 2 A. B. R. 466: "Under the English bankruptcy statutes (as well that of 1869 as those upon which our earlier acts were modeled), and our own bankruptcy statutes down to and including the Act of 1867, the making of a deed of general assignment was deemed to be repugnant to the policy of the bankruptcy laws, and, as a necessary consequence, constituted an act of bankruptcy per se. This is shown by an examination of the decisions bearing upon the point, both English and American. In *Globe Insurance Co. v. Cleveland Insurance Co.*, 14 Nat. Bankr. Reg. 311; 10 Fed. Cas., 488, the subject was ably reviewed and the authorities are there copiously collected. The decision in that case was expressly relied upon in *Re Beisenthal*, 14 Blatchf. 146, where it was held that a voluntary assignment, without preferences, valid under the laws of the State of New York, was void as against an assignee in bankruptcy, and this latter case was approvingly referred to in *Reed v. McIntyre*, 98 U. S. 513. So, also, in *Boese v. King*, 108 U. S. 379, 385, it was held, citing *Reed v. McIntyre*, that whatever might be the effect of a deed of general assignment for the benefit of creditors, when considered apart from the Bankruptcy Act, such a deed was repugnant to the object of a bankruptcy statute, and therefore was in and of itself alone an act of bankruptcy. The foregoing decisions related to deeds of general assignment made during the operation of the Bankruptcy Act of 1867, or the amendments thereto of 1874 and 1876. Neither, however, the Act of 1867, nor the amendments to it, contained an express provision that a deed of general assignment should be a conclusive act of bankruptcy. Such consequence was held to arise, from a deed of that description, as a legal result of the clause, in the Act of 1867, forbidding assignments with 'intent to delay, defraud, or hinder' creditors, and from the provision avoiding certain acts done to delay, defeat, or hinder the execution of the act."

Compare, inferentially, *Coal Land Co. v. Ruffner Bros.*, 21 A. B. R. 474 (C. C. A. W. Va.), though basing it upon another clause of § 67c: "In the present case, *Clark & Krebs*, creditors, had filed a petition against the *Cataract Colliery Company* in a State court of West Virginia, and in that proceeding the court had appointed a special receiver of the property of the said company. As above set forth, the *New River Coal Land Company* filed its answer and cross-bill in the suit and set up a claim thereby to the entire property of the *Colliery Company*, basing the claim on amounts alleged to be due for royalties accruing under a contract of lease, for taxes paid and for forfeiture of all said property as liquidated damages for the failure of the *Cataract Colliery Company* to fulfill the terms of said lease. The whole proceeding in the State court from the commencement of the action was within four months of the filing of the petition in bankruptcy and of the adjudication of the *Cataract Colliery Company* bankrupt. It is evident from the character of the suit and the condition of the *Colliery Company*, as disclosed by the pleadings, that at the time of the commencement of the suit it was insolvent;

61. Compare reasoning in *In re Gutwillig*, 1 A. B. R. 388, 92 Fed. 337 (C. C. A. N. Y., affirming 1 A. B. R. 78); *obiter*, *In re Congdon*, 11 A. B. R. 219

(D. C. Minn.). Compare, *Davis v. Bohle*, 1 A. B. R. 412, 92 Fed. 325 (C. C. A. Mo.), quoted *supra*.

it was unable to meet its obligations or to carry on its work, so alleged in the bill filed, and by the cross-bill of the Coal Land Company its entire property was claimed by one creditor to the exclusion of all others. The appointment by a court of a receiver for an insolvent debtor is an act of bankruptcy on the part of such debtor. Section 67c of the Bankrupt Act provides that a lien created by, or obtained in or pursuant to, any suit or proceeding at law, or in equity, including a judgment upon mesne process or a judgment by confession, which was begun against a person within four months before the filing of the petition in bankruptcy by or against such person, shall be dissolved by the adjudication of such person to be a bankrupt, if, first, it appears that said lien was obtained and permitted while the defendant was insolvent and that its existence and enforcement would work a preference."

There is no fatal weakness in the fact that all other parts of § 67 are taken up with attempts of single creditors, or creditors less than all, to get advantage over their fellows, whilst assignments and receiverships are presumably created for the equal benefit of all. Liens by legal proceedings, it will be remembered, are nullified by § 67 irrespective of their creating preferences.^{61a} Moreover, neither the principle of "*noscitur a sociis*" is violated nor that of "*in pari materia*," for § 67 is taken up with the broad subject of recovery of assets held by other courts, rather than with the narrower subject of the recovery of assets held by courts in behalf of some creditor seeking a selfish advantage.

Furthermore, the very wording of § 67 "c" avoiding liens created by legal proceedings within the four months' period where the same is "sought and permitted in fraud of the provisions of this Act," strikes precisely at such custody of the state courts as would take away from the bankruptcy courts the entire administration of the insolvent's estate. Indeed, frequently, when the basis of the superseding of the State Court's custody under receivers and assignees has been discussed, it has been placed upon such custody being a "fraud upon the Bankruptcy Act."⁶²

Instance, *In re Congdon*, 11 A. B. R. 219, 129 Fed. 478 (D. C. Minn.): "Assignments have generally been considered frauds on the Bankruptcy Law."

Instance, *In re Slomka*, 9 A. B. R. 637, 122 Fed. 630 (C. C. A. N. Y.): "Moreover, by the Bankrupt Law, the assignment was void having been executed within four months prior to the filing of the bankruptcy petition. Such a transfer by an insolvent debtor is made with intent to hinder, delay and defraud creditors because its necessary effect is to defeat the operation of the Bankrupt Act and the rights of creditors to such an administration of the assets of the debtor as that Act is intended to secure."

Obiter, *Singer v. Nat'l Bedstead Mfg. Co.*, 11 A. B. R. 285 (N. J. Ch.): "The debtor, other than a corporation, who undertakes to make a general assignment of his estate so that the same may be administered under a State law, is deliberately avoiding and evading the provisions of the Bankrupt Act, and is proceeding in defiance of its policy. He plainly is perpetrating a fraud on the act."

61a. Ante, § 1431.

62. Obiter, *Wilbur v. Watson*, 7 A. B. R. 55 (D. C. R. I.). Compare rulings under the act of 1867: *Ketcham*

v. McNamara, 6 A. B. R. 162, 72 Conn. 709. *Boese v. King*, 108 U. S. 379. *Reed v. McIntyre*, 98 U. S. 509.

It has been held in one case, though by a course of reasoning that seems somewhat too finely drawn, that the basis of the superseding is to be found, to be sure, in clause c of § 67, but not by virtue of receiverships being within any of the classes of liens by legal proceedings therein enumerated as dissolved unless dissolution thereof "would militate against the best interests of the estate;" that, on the contrary, the lien of the receivership would not be dissolved by the adjudication at all, but is simply "preserved" for the benefit of the trustee in bankruptcy, and without any order of preservation.

First Nat. Bank *v.* Guarantee Title, etc., Co., 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.): "By the appointment of a receiver by the State court on Sept. 12, 1906, upon a creditor's bill on the ground of insolvency, the receiver became vested with the rights of a levying creditor. * * * It must be conceded then, that between September 12, 1906, when the receiver was appointed by the State court, and September 29th, 1906, when the bankruptcy proceedings were commenced, the claim of the bank was subordinate to that of the receiver appointed by the State court. The question is, whether the lien, which that receiver had, passed to the trustee in bankruptcy. That question is to be determined by the Bankruptcy Act. Section 67c of the Bankruptcy Act is as follows: * * *

"The lien obtained by the receiver appointed by the State court was in a proceeding in equity begun against Jonathan A. Perley within four months before the filing of the petition in bankruptcy against him. It is obvious, therefore, that the lien may have been dissolved by the adjudication of bankruptcy if it was such a lien as is described in clause 1, clause 2, or clause 3 of the first sentence of 67c. We think each of these clauses refers to a lien obtained in a proceeding at law or in equity for the benefit, not of the bankrupt's creditors in general, but of one or more creditors less than all of them. If such be the proper construction of the first sentence of the section, it follows that the lien was not dissolved by force of any of its three clauses. But the second sentence of the section provides that, if the dissolution of 'such lien' would militate against the best interests of the estate of the bankrupt, the lien shall not be dissolved, but that the trustee shall be subrogated to the rights of the holder of the lien and empowered to perfect and enforce it as such holder might have done 'had not bankruptcy proceedings intervened.'

"If bankruptcy proceedings had not intervened, the receiver appointed by the State court could have perfected and enforced his lien. We think the words 'such lien,' in the second sentence of 67c, refer to any 'lien created by or obtained in or pursuant to any suit or proceeding at law or in equity,' mentioned at the beginning of the section, and not merely to a lien described by the language of clause 1, clause 2, or clause 3. It is not the intent of the section to dissolve a lien where its retention will benefit the general body of the bankrupt's creditors." Quoted further at § 1463.

It would seem, however, that the term "such lien," occurring in the clause, "Or if the dissolution of such lien would militate against the best interests of the estate," from its context naturally refers to none other than the three classes of liens therein enumerated as otherwise dissolved by the adjudication. Furthermore, the term "preserved" presupposes a lien otherwise "dissolved."

To be sure, if a corporation has been placed in the hands of a receiver at the suit of dissentient stockholders who are complaining of mismanage-

ment on the part of the directors and officers, though asserting its solvency notwithstanding, but is thereafter adjudged bankrupt within the four months of the receivership, undoubtedly the receivership would be superseded by the bankruptcy proceedings, since the rights of creditors would take precedence over those of dissentient stockholders, regardless of Bankruptcy Act, § 67, and if the corporation be insolvent nothing would remain for stockholders in any event; yet, such a situation could hardly arise on the state of facts mentioned, since the receivership would not itself be an act of bankruptcy, neither being on the "ground of insolvency" nor being the act of the corporation itself (though the corporation might in fact be insolvent), and so the corporation could not be forced into involuntary bankruptcy; whilst it would be equally barred from voluntary bankruptcy, since the functions of the directors, by the same hypothesis, would have been superseded by the receiver, the old board being incapacitated from the voluntary action requisite to voluntary bankruptcy.

§ 1604. Possession under General Assignments Superseded.—Thus, the possession of the State Court under an assignment for the benefit of creditors within the four months, is superseded.⁶³

§ 1605. Likewise, under State Court Receiverships.—Likewise the possession of the State Court under receiverships within the four months period, is superseded.⁶⁴

⁶³. In re Gutwillig, 1 A. B. R. 388, 92 Fed. 337 (C. C. A. N. Y.); Davis v. Bohle, 1 A. B. R. 412, 92 Fed. 325 (C. C. A. Mo.); In re Sievers, 1 A. B. R. 117, 91 Fed. 366 (D. C. N. Y.); In re Gray, 3 A. B. R. 647 (N. Y. Sup. Ct.); In re Knight, 11 A. B. R. 6, 125 Fed. 35 (D. C. Ky.); obiter, Leidigh Carriage Co. v. Stengel, 2 A. B. R. 383, 95 Fed. 645 (C. C. A. Ohio); In re Fellerath, 2 A. B. R. 40, 95 Fed. 121 (D. C. Ohio); In re Etheridge Furn. Co., 1 A. B. R. 115, 92 Fed. 329 (D. C. Ky.); obiter, In re Hirose, 12 A. B. R. 154 (D. C. Hawaii); obiter, In re Romanow, 1 A. B. R. 461, 92 Fed. 510 (D. C. Mass.); impliedly, In re Thompson, 11 A. B. R. 720, 128 Fed. 575 (C. C. A. N. Y.); In re Fish Bros. Wagon Co., 21 A. B. R. 147, 164 Fed. 553 (C. C. A. Kans.); Cohen v. American Surety Co., 20 A. B. R. 65 (C. C. A. N. Y.); impliedly, In re Farrell, 23 A. B. R. 826, 176 Fed. 503 (C. C. A. Ohio).

Creditors Committee Taking Possession and Selling without Bankrupt's Consent, a Conversion.—Again, if a creditors' committee takes charge of the bankrupt's assets, the bankrupt having absconded, and sells the same without the consent or ratification

of the bankrupt, it amounts to a conversion and the trustee in bankruptcy subsequently appointed may pursue the property or sue the committee for its value. In re Thomas-McNally Co., 29 A. B. R. 945, 208 Fed. 291 (D. C. N. Y.). See § 146.

⁶⁴. In re Knight, 11 A. B. R. 6, 125 Fed. 35 (D. C. Ky.), where the receivership was not the basis of the adjudication but a prior assignment was the basis.

In re Watts, 10 A. B. R. 113, 190 U. S. 1, in which case it seems to appear that perhaps the same rule would apply where the receivership or trusteeship was not the basis of the bankruptcy proceedings.

In re Brown, 1 A. B. R. 110, 91 Fed. 358 (D. C. Ore.).

Receiverships Amounting to State Bankruptcy and State Insolvency Proceedings.—For cases involving receiverships but where the receiverships amounted, in effect, to State Bankruptcy or State Insolvency proceedings, and therefore come rather under the next division, division 3 of chapter XXXII, relative to the superseding of State Bankruptcy and State Insolvency proceedings; see foot-note to the main

Thus, a suit for the dissolution of a partnership instituted within the four months may be superseded.

Wilson v. Parr, 8 A. B. R. 230, 115 Ga. 629: "In such a case it is not erroneous for a superior court, which had within four months prior to the adjudication in bankruptcy appointed a receiver to take charge of and administer the assets of such partnership, to grant an application that the receiver deliver those assets to the trustee in bankruptcy."

But it will not be superseded where it was instituted before the four months.⁶⁵

Obiter, In re Rogers & Stefani, 19 A. B. R. 566, 156 Fed. 267 (D. C. Ark.): "In this case the said chancery court acquired jurisdiction of the persons and property of Rogers and Stefani, the bankrupts, more than four months before the proceedings in bankruptcy were begun, and if it had retained possession of the property until the order in controversy was made, it would not have lost control of the property by the adjudication in bankruptcy."

§ 1606. General Assignment Not Per Se Illegal nor Void but Voidable Merely.—General assignments for the benefit of creditors are valid until bankruptcy intervenes. They are not per se illegal; they are voidable, not void.⁶⁶

proposition of this division, ante, § 1602.

Dissolution of Corporations.—For cases of receiverships in proceedings for the dissolution of corporations, see post, division 3, § 1634, and ante, §§ 150 to 159, inclusive.

Receiverships incidental to foreclosure and other equity proceedings, see ante, § 1586.

Mauran v. Carpet Lining Co., 6 A. B. R. 734, 50 Atl. 331 (R. I. Sup. Ct.): The decision in this case was based on both grounds, § 67 (f), and on the fact that the receivership amounted to State Bankruptcy or State Insolvency proceedings.

Impliedly, In re Tyler, 5 A. B. R. 152, 104 Fed. 778 (D. C. N. Y.); instance, In re Hecox, 21 A. B. R. 314, 164 Fed. 823 (C. C. A. Colo.), quoted on other point at § 1611; compare, *obiter*, *Scheuer v. Book Co.*, 7 A. B. R. 384, 112 Fed. 384 (C. C. A. Ala.). But compare, *Strohl v. Sup. Ct.*, 2 A. B. R. 92 (Sup. Ct. Wash.).

New River Coal Land Co. v. Ruffner Bros., 21 A. B. R. 474, 165 Fed. 881 (C. C. A. W. Va.), quoted at § 1603. Compare, In re Electric Supply Co., 23 A. B. R. 647, 175 Fed. 612 (D. C. Ga.),

First Nat. Bk. v. Title Guarantee, etc., Co., 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.), quoted and

discussed at § 1603; In re Standard, etc., Co., 26 A. B. R. 562, 186 Fed. 578 (D. C. Ala.); In re Zeigler Co., 26 A. B. R. 761, 189 Fed. 259 (D. C. Conn.).

⁶⁵ In re Price, 1 A. B. R. 609, 92 Fed. 987 (D. C. N. Y.); In re Carver & Co., 7 A. B. R. 539, 113 Fed. 128 (D. C. N. Car.). But compare, In re Price, 1 A. B. R. 609, 92 Fed. 987 (D. C. N. Y.).

Compare, also In re Sterlingworth Ry. Supply Co., 21 A. B. R. 342, 164 Fed. 591, 165 Fed. 267 (D. C. Pa.), where the bankruptcy court refused to supersede the State court, but not on the ground of the four months limit, but rather because the assets had been in the State receiver's hands for more than a year, and because it was more advantageous to let the State court continue.

⁶⁶ *Grunsfeld Bros. v. Brownell*, 11 A. B. R. 602 (New Mex. Sup. Ct.); In re Carver & Co., 7 A. B. R. 541 (D. C. N. Car.).

Contra, and that their necessary effect, is to hinder, delay and defraud creditors, see In re Salmon & Salmon, 16 A. B. R. 122, 143 Fed. 395 (D. C. Mo.). Also, contra, *Rumsey v. Machine Co.*, 3 A. B. R. 704, 99 Fed. 699 (D. C. Mo.).

Pro, but in a dissenting opinion, *Cohen v. American Surety Co.*, 22 A. B. R. 909, 132 App. Div. (N. Y.) 917.

Randolph v. Scruggs, 190 U. S. 533, 10 A. B. R. 3: "The assignment was not illegal. It was permitted by the law of the State, and cannot be taken to have been prohibited by the Bankruptcy law absolutely and in any event. It had no general fraudulent intent. It was voidable only in case bankruptcy proceedings should be begun."

Summers v. Abbott, 10 A. B. R. 258, 122 Fed. 36 (C. C. A. Mo.): "The deed of assignment covered all the property of the bankrupts. It was honestly made for the laudable purpose of applying all the property of the debtors to the payment, ratably, of all their debts. This is conceded. No claim is made that there was a secret trust reserved for the grantor's benefit, or that there was otherwise any fraud in fact in the execution and delivery of the deed. It was not made to hinder, delay, or defraud creditors, but to pay creditors. Fraud cannot be predicated of such a deed. It constituted an act of bankruptcy, which entitled the debtor's creditors, if they saw proper to do so, to have the administration of the trust transferred from the assignee to the bankrupt court, but this is no impeachment of the honesty of the transaction; and the debtors, when adjudged bankrupts, would be entitled to their discharge, precisely as though they had made no such assignment. It is also admitted that the appellant, who was named in the deed as assignee, accepted the trust in good faith, and for the purpose of executing it according to law and the terms of the deed; and that he did execute it intelligently, successfully, and honestly, is conceded. Neither fraud in fact nor in law can be imputed to such an assignee.

"The contention of the trustee in bankruptcy is that all assignments for the benefit of creditors since the passage of the Bankrupt Act are fraudulent, and that every assignee under such a deed is a fraudulent vendee or assignee, and hence entitled to no compensation for his services. This contention is probably grounded on the assumption that it is the legal duty of an insolvent debtor who wants to apply his property to the payment of his debts to apply to the bankrupt court to be adjudged a bankrupt, and then turn his property over to the trustee of his estate in bankruptcy. But neither in the present nor any previous Bankrupt Law this country has ever had will there be found any provision making it obligatory upon a debtor to go into court and have himself adjudged a bankrupt. The Bankrupt Act declares the making of 'a general assignment for the benefit of his creditors' shall constitute an act of bankruptcy, but it nowhere declares that when the debtor has committed an act of bankruptcy he shall go into the bankrupt court and have himself adjudged a bankrupt. Many debtors who commit acts of bankruptcy struggle on and finally pay all the debts they owe, which is much more than would have been done had they gone into the bankrupt court and had themselves adjudged bankrupts. It is open to the creditors of one who has committed an act of bankruptcy to proceed to have him adjudged a bankrupt, but it is optional and not obligatory upon his creditors to do this. As a matter of fact, thousands of debtors commit acts of bankruptcy who are never adjudged bankrupts; their creditors preferring to let their debtor administer his own estate, rather than turn it over to a bankrupt court."

In *re Chase*, 10 A. B. R. 677, 124 Fed. 753 (C. C. A. R. I.): "That there was nothing unlawful in such an assignment, but that it was merely voidable by proceedings in bankruptcy, and meritorious unless avoided, has been clearly affirmed by the Supreme Court under the prior statutes. * * *

"Nothing in these expressions of the Supreme Court declares that general assignments, honestly made, are contrary, to the policy of the bankruptcy statutes; and, on the other hand, they are declared to be in harmony therewith."

In *re Sievers*, 1 A. B. R. 117, 91 Fed. 366 (D. C. Mo., affirmed, sub nom. Davis

v. Bohle, 1 A. B. R. 412: "It results from these views that while proceedings under the insolvency laws, as such, are now void, whether proceedings in bankruptcy follow or not, proceedings under the general assignment laws of States like Missouri, or under the common-law deed of assignment, are not void or voidable, unless proceedings in bankruptcy are subsequently instituted, and whether such is the case when an adjudication in bankruptcy follows, is now to be considered."

Obiter (being case of act of bankruptcy) In *re Hirose*, 12 A. B. R. 154 (D. C. Hawaii): "There being no insolvent laws in the Territory of Hawaii, assignments for the benefit of creditors are good, under the common law, for all purposes except against proceedings in bankruptcy instituted under the Bankrupt Act within four months of their execution."

"If under such proceedings, the respondent is declared bankrupt, the assignment becomes void and the bankrupt's property is thereby transferred to the jurisdiction of the court of bankruptcy."

Obiter (being case of act of bankruptcy) In *re Romanow*, 1 A. B. R. 461, 92 Fed. 510 (C. C. A. Mo.): "Though the assignment is an act of bankruptcy, and is avoided by the adjudication, yet it is not a void instrument, but only a voidable one and until adjudication it is valid."

But where the general assignment statute is, in effect, an insolvency statute, then the rules as to the suspension of state insolvency or bankruptcy laws will prevail.⁶⁷

In *re Curtis*, 1 A. B. R. 440, 91 Fed. 737 (D. C. Ills.): "And proceedings under it are void and not merely voidable."

§ 1607. Unless Petition Filed within Four Months, Followed by Adjudication, State Court's Custody Not Superseded.—Unless bankruptcy proceedings are instituted within the prescribed four months after an assignment or receivership and adjudication of bankruptcy follows, the bankruptcy will not operate to supersede the control of the state court over the assignment or receivership proceedings, and the state court will retain jurisdiction over the property until its administration is completed.⁶⁸

§ 1608. But if Filed within Four Months and Adjudication Occurs, Assignment Void.—But when bankruptcy intervenes within four months after a general assignment, the general assignment is void.⁶⁹

§ 1609. Until Adjudication, Custody Not Superseded.—Until adjudication, however, the custody of the state court cannot be superseded. The mere filing of the petition will not give jurisdiction to the bankruptcy court to supersede the state court.⁷⁰

⁶⁷. In *re Smith & Dodson*, 2 A. B. R. 9 (D. C. Ind.). Compare, post, division 3, this chapter, § 1627, et seq.

⁶⁸. In *re Shinn*, 25 A. B. R. 833, 185 Fed. 990 (D. C. N. J.). See cases cited under main proposition of this chapter, under the section relating to "Assignments and Receiverships Created before the Four Months," § 1594. Also, cases cited under §§ 1602, 1603.

In *re Farrell*, 23 A. B. R. 26, 176 Fed. 505 (C. C. A. Ohio), quoted, on other points, at § 1632; *Eyster v. Gaff*, 91 U. S. 591; *Boese v. King*, 108 U. S. 379.

⁶⁹. See cases under main proposition, ante, §§ 1602, 1603.

⁷⁰. Compare, inferentially, In *re Kersten*, 6 A. B. R. 517, 110 Fed. 929 (D. C. Wis.). Also, see ante, § 1600. State ex rel. *Strohl v. Sup. Ct.*, 2 A. B. R. 97

§ 1610. Assignee or Receiver May Be Enjoined.—The assignee or receiver may be enjoined.⁷¹

Obiter, Carling v. Seymour Lbr. Co., 8 A. B. R. 41, 113 Fed. 483 (C. C. A. Ga.): "While it is a general rule that a Federal court may not enjoin proceedings in a State court, an exception is made in cases where such injunction may be authorized by any law relating to proceedings in bankruptcy. Rev. Stat., U. S., § 720. When the State court is in possession through its receiver, of assets that it is without jurisdiction or authority to hold against a receiver or trustee appointed in bankruptcy proceedings, instead of making a peremptory order on the receiver of the State court to surrender the funds an injunction, if necessary, might be granted by the bankruptcy court to prevent the unlawful distribution of the assets, until application could be made to the State court for an order to its receiver to surrender the assets to the proper custodian. The laws of the United States being equally binding on all the courts, we cannot assume that the State court would refuse to administer them. We are not now called on to decide what course should be taken in the event of a disregard of the Bankrupt Law by the State court."

New River Coal Land Co. v. Ruffner Bros., 21 A. B. R. 474, 165 Fed. 881 (C. C. A. W. Va.): "In an act forbidding courts of the United States to stay proceedings in a State court the courts of bankruptcy are specifically excepted and the bankruptcy law of 1898 expressly confers upon these courts the power to issue injunctions to stay proceedings within this exception. * * * The prime purpose of the Bankruptcy Act is to secure an equal distribution of an insolvent's estate among the creditors, and it is not only a power conferred upon the court in a bankruptcy proceeding to take jurisdiction of the unencumbered property of a bankrupt, but also of property to which liens attach, provided the judge of the court in bankruptcy shall determine that such property should be administered by that court. It has not unfrequently been the case that the bankrupt courts have issued injunctions to stay proceedings in a State court, to foreclose mortgages, to enforce other liens, and even to forbid State officers from proceeding with executions upon judgments, where in the opinion of the judge of the bankruptcy court, it was to the interest of the general estate to do so."

§ 1611. May Be Ordered Summarily to Surrender Assets.—And the assignee or receiver may, after the adjudication of bankruptcy, be required by the bankruptcy court to surrender the assets to the trustee in bankruptcy; and the assignee or receiver may be so required by summary order from the bankruptcy court.⁷²

(Sup. Ct. Wash.). But compare (this principle evidently overlooked), *In re Zeigler Co.*, 26 A. B. R. 761, 189 Fed. 259 (D. C. Conn.), in which case the proper remedy would have been an injunction.

^{71.} *In re Gutwillig*, 1 A. B. R. 388, 92 Fed. 337 (C. C. A. N. Y.); *Leidigh Carriage Co. v. Stengel*, 2 A. B. R. 383, 95 Fed. 637 (C. C. A. Ohio); *West Co. v. Lea*, 2 A. B. R. 467, 174 U. S. 590; *Davis v. Bohle*, 1 A. B. R. 412, 92 Fed. 325 (C. C. A. Mo.).

Compare, analogous ruling as to custodians and court officers in pos-

session under nullified legal liens, ante, § 1473. Also, custodians and court officers in possession under nullified legal liens not adverse parties, post, § 1827. Also, see ante, § 359; and post, § 1901, et seq.

^{72.} See post, § 1830. *In re Smith & Dodson*, 2 A. B. R. 9 (D. C. Ind.); *In re Fellerath*, 2 A. B. R. 40, 95 Fed. 121 (D. C. Ohio.); *In re Thompson*, 11 A. B. R. 719, 128 Fed. 575 (C. C. A. N. Y., affirming 10 A. B. R. 242); compare, *In re Carver & Co.*, 7 A. B. R. 539, 113 Fed. 138 (D. C. N. Car.); *In re Stokes*, 6 A. B. R. 262, 106 Fed. 312

In *re Hecox*, 21 A. B. R. 314, 164 Fed. 823 (C. C. A. Colo.): "By operation of law, on the adjudication in bankruptcy and the selection and qualification of a trustee, all right, title, and interest of the bankrupt in and to any and all property passed to and vested in such trustee. The scheme as well as the policy of the Bankrupt Act is that the collecting, marshaling, administration, and distribution of the bankrupt's estate shall reside exclusively in the court of bankruptcy. As the Bankrupt Act is a national law, enacted pursuant to the power vested by the Constitution in Congress, it is a paramount law of the land, to which all State authority, legislative and judicial, must submit. As the receiver in question was appointed by the State court within four months next preceding the filing of the petition in bankruptcy, the debtor being insolvent, his appointment constituted an act of bankruptcy. In contemplation of the Bankrupt Act, in so far as concerned his right to the custody of the property of the bankrupt, he stood as if he had never been appointed by the State court. In such situation, as he holds the property not in his own right, but solely in his claimed official capacity, it was his duty, on notification and demand by the trustee in bankruptcy, to deliver the property to him. But inasmuch as he was the appointee of the State court, as a mere act of courtesy, sometimes, but hardly accurately, termed 'judicial comity,' the bankrupt court in the first instance directed the trustee to prefer a request of the State court for an order on its receiver to deliver the property in his custody to the trustee. In such case, if the State court decline to reciprocate the consideration thus paid to its dignity, the law is well settled that it is then competent for, and the duty of, the bankrupt court to order the receiver to deliver the property over to the trustee, and he would be in contempt if he refuses to comply therewith. Controlling authorities affirm the foregoing propositions."

And the rule applies though the assignment be not one by formal deed of assignment; as, for example, in cases of trust arrangements for effecting compositions out of court.

Obiter, In *re Hersey*, 22 A. B. R. 856, 171 Fed. 998 (D. C. Iowa): "The instrument provides that Hart shall be first paid from the proceeds of the sale of the property for his services and for the expenses * * * incurred by him in caring for and disposing of the same, and in effecting a settlement

(D. C. Penn.); In *re Farrell*, 23 A. B. R. 826, 176 Fed. 505 (C. C. A. Ohio); In *re Zeigler Co.*, 26 A. B. R. 761, 189 Fed. 259 (D. C. Conn.); In *re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio), quoted at § 1665 and at § 1827.

Apparently contra, as to summary jurisdiction, In *re Manning*, 10 A. B. R. 497, 123 Fed. 180 (D. C. S. D.). But the facts in this case show the funds had already been disbursed as to which the summary order was sought.

Compare similar rules as to custodians and Court officers in possession under nullified legal liens, ante, § 1474, and under "Agents Not Adverse Parties," § 1822.

The Supreme Court in the case of *Louisville Trust Co. v. Cominger*, 184 U. S. 18, 7 A. B. R. 421, affirming *Sinsheimer v. Simonson*, 5 A. B. R. 537, is not contra, for there the as-

signee was claiming, as an individual, right to retain his commissions, etc.

But the assignee of a partnership will not be required to surrender the partnership property in his hands to the trustee in bankruptcy of the individual members, In *re Mercur*, 10 A. B. R. 505, 122 Fed. 384 (C. C. A. Penn., affirming 8 A. B. R. 275).

Compare, *Ludowici Tile Roofing Co. v. Penn. Inst.*, 8 A. B. R. 739 (D. C. Penn.): "A trustee of individual partners has no right to interfere with firm assets."

But the assignee of an individual partner will be required to surrender the individual assets, by summary order, to the trustee in bankruptcy of the partnership itself, on the partnership's subsequently becoming bankrupt, In *re Stokes*, 6 A. B. R. 262, 106 Fed. 312 (D. C. Penn.).

with the creditors of the bankrupt, or in attempting to do so. While the instrument is not an 'assignment' under the State statute for the benefit of creditors, such is its effect, and Hart thereunder was but the agent of the bankrupt, with the rights given him by the instrument, for the sale of the property and distribution of its proceeds as provided therein."

Of course, plenary action may be instituted, instead.⁷³

§ 1611½. But Only on Due Notice and Hearing.—But such summary order may be granted only upon notice and after due hearing; and the rule is not different, in this regard, where such assignee or receiver has been elected trustee in the subsequent bankruptcy.

Loveless v. Southern Grocer Co. Lim., 20 A. B. R. 180, 159 Fed. 415 (C. C. A. La.): "The record shows, without dispute, that the trustee, as such, had paid out in costs and dividends about \$1,300 under orders of the bankruptcy court. The summary order requiring him to make payment into the bankruptcy court raises a controversy as to \$660.34. This sum, or most of it, petitioner claims that he paid out legally and properly while he was acting as receiver in the State court, and his contention is that he should not be required to pay the money again, and, at least, that he should not be required by a summary proceeding to pay the money into the bankruptcy court without a hearing, either in that court or in the bankruptcy court, on the question as to whether or not he is entitled to credits for the payments made by him as receiver. The question as to the correctness of these disbursements has not been passed on by the State court, nor by the court below, and, of course, is not before this court for decision. We are asked to review and vacate or correct the summary order of the court below requiring the payment of the sum in dispute into court before the petitioner has had a hearing on the correctness of his accounts and the legality of the contested disbursement. If the order to pay the money into courts stands, summary proceeding against the trustee can be made the basis of proceedings for contempt if he fails to obey the order. It seems to us just and right that he should have an opportunity to present his accounts to a court and to have his claim for credits for payments made by him while receiver in the State court passed on. He should not be required to pay the money into court by a summary proceeding that deprives him of the right to a hearing on the disputed items of his account. It is true that the bankruptcy proceedings operated to suspend the further administration of the insolvent corporation's estate in the State court; 'but it remained for the State court to transfer the assets, settle the accounts of its receiver, and close its connection with the matter. Errors, if any, committed in so doing, could be rectified in due course and in the designated way.'"

§ 1612. No Summary Order as to Sums Already Disbursed.—In no event, however, may the assignee be required by summary order of the bankruptcy court, to account for (in the sense of paying over the equivalent of) disbursements already made before the filing of the petition in bankruptcy.⁷⁴

⁷³. Instance, *Cohen v. American Surety Co.*, 22 A. B. R. 909, 132 App. Div. (N. Y.) 917.

⁷⁴. See § 1830. In *re Manning*, 10 A. B. R. 497, 123 Fed. 180 (D. C. S. Car.). See post, § 1829. Compare, *Loveless v. Southern Grocer Co. Lim.*,

20 A. B. R. 180, 159 Fed. 415 (C. C. A. La.), quoted, on other points, § 1611½; *Obiter* and impliedly, In *re Hays*, 24 A. B. R. 979, 181 Fed. 674 (C. C. A. Ohio), quoted at § 1665 and at § 1827.

In *re Klein & Co.*, 8 A. B. R. 559, 116 Fed. 523 (D. C. N. Y.): "There can be no doubt that the court acquired full jurisdiction of such of the bankrupt estate as was in the possession of or under control of the assignee when the petition was filed, but if the funds had been disbursed before that time and had passed beyond the control of the assignee, it does not seem that they formed a part of the bankrupt's estate which fell under the jurisdiction of this court, even though the assignee submitted himself to the jurisdiction with respect to his accounts."

Nor for commissions retained and spent by him before then.⁷⁵

Louisville Trust Co. v. Comingor, 184 U. S. 18, 7 A. B. R. 421, the syllabus of which reads: "An assignee for the benefit of creditors has the right to have his claims for the amount paid to counsel or retained by him on account of commissions as assignee before the bankruptcy of the assignor adjudicated in the State Court in the customary mode of proceeding, and the bankruptcy court has no jurisdiction to finally adjudicate the merits of his claims unless by his consent and then only by plenary suit."

Nor may he be required to account for disbursements made by him before the four months;⁷⁶ but probably he may be required to account for commissions retained by him after the bankruptcy,⁷⁷ although a transferee under an instrument for effecting a composition out of court has been held not within summary jurisdiction as to moneys retained by him for expenses and compensation, even though subject thereto for the remaining assets in his control.⁷⁸ And the rule is not altered because of the assignee's voluntary offer to account.⁷⁹

As to sums already disbursed, the assignee is to be reached only by plenary action in the State court, or in case of diversity of citizenship, etc., in the United States District Court.⁸⁰

§ 1613. Sales by Assignee under Void Assignment.—Sales made by the assignee under the void assignment may be set aside by the bankruptcy court for sufficient cause; probably, however, only where the state court in charge of the assignment would have had jurisdiction to set them aside.⁸¹ Thus, the title to property sold by the assignee but not paid for,

⁷⁵. In *re Klein & Co.*, 8 A. B. R. 559, 116 Fed. 523 (D. C. N. Y.), in which case the court extends the rule of disbursements made even up to the time of the filing of the petition against the assignee to call him to an accounting. *Sinsheimer v. Simonson*, 5 A. B. R. 537, 107 Fed. 898 (C. C. A. Ky.), affirmed sub nom. *Louisville Trust Co. v. Comingor*, 7 A. B. R. 421, 184 U. S. 18; In *re Scholtz*, 5 A. B. R. 782, 106 Fed. 834 (D. C. Iowa). Obiter and inferentially, In *re Hays*, 24 A. B. R. 979, 181 Fed. 674 (C. C. A. Ohio), quoted at § 1665.

⁷⁶. In *re Carver & Co.*, 7 A. B. R. 539, 113 Fed. 138 (D. C. N. Car.).

⁷⁷. Inferentially, In *re Thompson*, 11 A. B. R. 720, 128 Fed. 575 (C. C.

A. N. Y.). Instance, In *re Banzai Mfg. Co.*, 25 A. B. R. 497, 183 Fed. 298 (C. C. A. N. Y.); instance, but not based wholly on this ground, In *re Hays*, 24 A. B. R. 979, 181 Fed. 674 (C. C. A. Ohio), quoted at § 1665 and at § 1827.

⁷⁸. In *re Hersey*, 22 A. B. R. 856, 171 Fed. 998 (D. C. Iowa).

⁷⁹. In *re Klein & Co.*, 8 A. B. R. 559, 116 Fed. 523 (D. C. N. Y.).

⁸⁰. Instance (partly), dissenting opinion, *Cohen v. American Surety Co.*, 22 A. B. R. 909, 132 App. Div. (N. Y.) 917.

⁸¹. Compare, impliedly, In *re Finlay Bros.*, 4 A. B. R. 745, 104 Fed. 675 (D. C. N. Y.); impliedly, In *re Knight*, 11 A. B. R. 1, 125 Fed. 35 (D. C. Ky.).

passes to the trustee,⁸² but the property may not be recovered, except by plenary action.

In *re Findlay Bros.*, 4 A. B. R. 745, 104 Fed. 675 (D. C. N. Y.): "Assuming, as contended by the creditors, that the money used by the bankrupts' wives to purchase the stock, was the money paid to them by the bankrupts before the institution of bankruptcy proceedings, still under the decision of the Supreme Court in the case of *Bardes v. Bank* (178 U. S. 524, 4 Am. B. R. 163), the payment of those moneys by the wives for the stock could not be disregarded, nor could the money be retained by the trustee upon setting aside the sale, but it would have to be returned. * * * For any relief, supposing I were to grant an order setting aside the sale, a bill in equity must be filed in the State court for an accounting as respects the goods or their proceeds, to which all persons concerned in the disposition of the goods subsequent to the sale and against whom relief was sought, would be necessary parties. After this lapse of time and the various changes that have occurred, I think the prosecution of such a suit would be attended with much labor and expense, and looking at all the circumstances, I have so much doubt as respects any beneficial final result, that I think I ought not to set aside the sale except upon security given by the creditors to indemnify the trustee against any loss or expense occasioned thereby, or by the subsequent proceedings to recover assets."

§ 1614. Assignee Has Lien upon Surrendered Assets for Expenses and Compensation.—When the bankruptcy court takes over the assets from the state court which has been administering the assignment, the assets come over subject to a lien for the reasonable expenses and compensation of the assignee, incurred or earned while performing services beneficial to the estate and necessary to its preservation, where the assignment was bona fide.⁸³

⁸². In *re Knight*, 11 A. B. R. 1, 125 Fed. 35 (D. C. Ky.).

⁸³. *Summers v. Abbott*, 10 A. B. R. 254, 122 Fed. 36 (C. C. A. Mo.); impliedly, In *re Levitt*, 11 A. B. R. 411 (D. C. Wis.). Compare, to same general effect, In *re Bussey*, 6 A. B. R. 603 (Ref. Mo.); In *re Scholtz*, 5 A. B. R. 782, 106 Fed. 834 (D. C. Iowa); In *re Pauly*, 2 A. B. R. 333 (Ref. N. Y.). Impliedly, In *re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio), quoted on entirely different point at § 1665.

Compare, to same conclusion, In *re Klein & Co.*, 8 A. B. R. 559 (D. C. N. Y.): This decision is placed upon the ground that creditors, having permitted the assignee to go ahead and administer the estate in the insolvency court, are bound to reimburse him therefor. This might be good ground for holding those who did so permit him to proceed and therefore might be held to have assented thereto, but how about those who objected and dissented and did their best

to get enough creditors together to file a petition in bankruptcy?

Compare, In *re Pattee*, 16 A. B. R. 450, 143 Fed. 994 (D. C. Conn.), where an assignee was allowed compensation and reimbursement for what was done after bankruptcy proceedings were instituted but not for what was done before: being directed to present the latter as a "claim."

Rulings on Assignee's Claims in Bankruptcy before *Randolph v. Scruggs*.—Before the Supreme Court announced its decision in *Randolph v. Scruggs*, 190 U. S. 533; S. C., 10 A. B. R. 1, *supra*, there were various contrary holdings, to the effect that an assignee for the benefit of creditors was not entitled to reimbursement for expenses nor compensation as assignee incurred nor earned before the filing of the bankruptcy petition; inasmuch as they were incurred with the full knowledge that an act of bankruptcy was being committed, and that the assignment was likely to be nullified; also because the Bank-

Randolph v. Scruggs, 190 U. S. 533, 10 A. B. R. 1: "The assignment was not illegal. It was permitted by the law of the State, and cannot be taken to have been prohibited by the bankruptcy law absolutely in every event, whether proceedings were instituted or not. * * * It seems to us that it would be a hard and subtle construction to say, as seems to have been thought in *Bartlett v. Bramhall*, 3 Gray 257, 260, that when they were instituted they not only avoided the assignment, but made it illegal by relation back to its date, when, if they had not been started, it would have remained perfectly good."

In *re Chase*, 10 A. B. R. 677, 124 Fed. 753 (C. C. A. R. I., reversing In *re Gladding*, 9 A. B. R. 171 [Ref. R. I.] and in effect overruling *Wilbur v. Watson*, 7 A. B. R. 54): "In the present case, the claims of petitioners constituted a lien on the assets in their hands adverse to the trustee, and the portion of the statute cited appertains to nothing of that nature. * * *

"The fact that, under the circumstances, the petitioners paid the trustee the gross amount received by them, and delivered them the other assets, does not, as is clearly settled, deprive them of the right to apply to the court for payment of the sums for which they once had a lien."

§ 1615. Assignment Must Be "General" and "Bona Fide" Not "Partial" nor "Fraudulent."—But the assignment must be a general assignment for the equal benefit of all creditors, and not a partial nor preferential assignment, and must be bona fide, else the lien will not attach.

ruptcy Act itself limits reimbursement for the preservation of the estate to expenses incurred subsequently to the filing of the petition.

In *re Peter Paul Book Co.*, 5 A. B. R. 105, 104 Fed. 786 (D. C. N. Y.); In *re Gilblom & King*, 2 N. B. N. & R. 60 (Ref. Ohio); In *re Mays*, 7 A. B. R. 764 (D. C. W. Va.); *Stearns v. Flick*, 4 A. B. R. 723, 103 Fed. 921 (D. C. Ohio); In *re Tatem, Mann & Co.*, 7 A. B. R. 52, 112 Fed. 50 (D. C. N. Car.); *Wilbur v. Watson*, 7 A. B. R. 54, 111 Fed. 493 (D. C. R. I.). In this connection, see In *re Gladding*, 9 A. B. R. 171 (Ref. R. I.), reversed by C. C. A. sub nom. In *re Chase*, 10 A. B. R. 677, 124 Fed. 753 (C. C. A. R. I.). Also, see In *re Kingman*, 5 A. B. R. 251 (Ref. Mass.).

But even before the Supreme Court's decision in *Randolph v. Scruggs* there were various holdings to the same effect: In *re Bussey*, 6 A. B. R. 603 (Ref. Mo.); In *re Schlotz*, 5 A. B. R. 782, 106 Fed. 834 (D. C. Iowa); In *re Klein & Co.*, 8 A. B. R. 559, 116 Fed. 523 (D. C. N. Y.); In *re Pauly*, 2 A. B. R. 333 (Ref. N. Y.).

However, it was held that such assignee should be allowed to prove his claim as a general claim against the estate and be allowed to share in the dividends therefrom the same as any other agent to whom the bankrupt before bankruptcy might have entrusted

his property for care and distribution. In *re Gilblom & King*, 2 N. B. N. & R. 60 (Ref. Ohio); In *re Mays*, 7 A. B. R. 764 (D. C. W. Va.); Impliedly, In *re Tatem, Mann & Co.*, 7 A. B. R. 52, 112 Fed. 50 (D. C. N. Car.).

Year's Limitation for Proof of Claims Does Not Apply to Assignee's Lien.—The assignee's claim is not a claim within the meaning of § 57 (n) prohibiting proofs of claims after the expiration of a year from the date of adjudication; nor a "debt," as defined by § 1, In *re Levitt*, 11 A. B. R. 411 (D. C. Wis.).

Pledge Redeemed by Assignee.—In *re William W. Rudd*, 25 A. B. R. 35, 180 Fed. 312 (D. C. N. Y.): "A pledge redeemed from a pawnbroker by a third party (in this case by an assignee for the benefit of creditors) is no longer the subject of the pawnbroker's lien, as the person redeeming it is not qualified to act as pawnbroker. Nor do the State laws give a statutory lien to any person who may pay something for the account of another, even if personal property, may pass as security for the account. But the doctrine of subrogation is well-established, and a court of equity, or even a court of law, would accept the proposition that if a third party pays a debt, and takes into his own possession personal property which has been held as security."

The decisions generally qualify the doctrine by saying an assignment "honestly" made.

In *re Chase*, 10 A. B. R. 677, 124 Fed. 753 (C. C. A. R. I.): "No criticism is made of the terms of the assignment nor any suggestion that it was not framed in all respects for the advantage of all the creditors."

Summers v. Abbott, 10 A. B. R. 254, 122 Fed. 36 (C. C. A. Mo.): "To prevent misapprehension it is proper to say that this case has none of the odious features about it that sometimes crops out in cases where insolvents make deeds of assignment for the professed benefit of their creditors, but which are in fact made to embarrass and defraud them, and where the assignee is a willing instrument of the fraudulent debtor."

Randolph v. Scruggs, 190 U. S. 533, 10 A. B. R. 1: "The assignment has no general fraudulent intent; mere constructive fraud in an assignment for the equal benefit of all creditors is not a bar to the assignee's receiving compensation, though the case would be different if the assignee were a party to actual fraud."

In *re Harson Co.*, 11 A. B. R. 516 (Ref. R. I.): "In all three of the above cases it is to be noted, however, that the assignment was for the equal benefit of all creditors, while the question now before us is whether an assignment which was for the benefit only of such creditors as chose to assent to receive in full satisfaction, whatever the assignee paid them, is on the same footing. The assignee contends that this was not a preferential assignment. But that an assignment which is so drawn is preferential seems to be the settled law even where such an assignment is held good."

When will the court decide the assignment is not within the rule because *not* "honestly" made? One case, In *re Congdon*, 11 A. B. R. 219 (D. C. Minn.) held that, under the circumstances of that case, the assignment was fraudulent, the bankrupt being left in charge of his store, to run it, on a salary, under an agreement that the stock should be replenished from time to time; in addition to which the assignment deed itself was peculiar; and, finally, all parties knew bankruptcy proceedings were inevitable.

It must not be partial nor preferential.⁸⁴ But that the assignment provides, in accordance with the state law, permission that only those may participate in its benefits who consent to the debtor's release from his remaining debts, would not necessarily make it fraudulent.⁸⁵

It is none the less "general" though expressly limited to be for the benefit of creditors becoming parties and signing the agreement.⁸⁶

It is not essential that the assignment shall have been an assignment by a formal deed.⁸⁷

§ 1616. Receivers Likewise Entitled to Lien Where Receiver-ships Nullified by Bankruptcy.—The same rule applies in cases of re-

⁸⁴ In *re Harson Co.*, 11 A. B. R. 516 (Ref. R. I.). Compare, In *re Wertheimer*, 6 A. B. R. 187 (Ref. N. Y.).

When Is an Assignment "General," When "Partial?"—See ante, § 146.

⁸⁵ Compare, analogously, *Patty-*

Joinder Co. v. Cummings, 4 A. B. R. 272 (C. C. A. Tex.).

⁸⁶ In *re Courtenay Mercantile Co.*, 26 A. B. R. 365, 186 Fed. 352 (D. C. N. Dak.), quoted ante at § 146.

⁸⁷ See post, § 1617½; In *re Hersey*, 22 A. B. R. 856, 171 Fed. 998 (D. C. Iowa).

ceiverships and trusteeships rendered void by subsequent bankruptcy proceedings under the Amendment of 1903 making such receiverships and trusteeships acts of bankruptcy; provided the receiver or trustee were appointed for the general benefit of all creditors.⁸⁸

In *re Zier & Co.*, 15 A. B. R. 648, 142 Fed. 102 (C. C. A. Ind., affirming 11 A. B. R. 527): "The bankruptcy jurisdiction when properly invoked, supercedes the prior proceedings in the State court for winding up the corporation, 'as to which the jurisdiction is not concurrent' (In *re Watts and Sachs*, 190 U. S. 1, 27, 10 Am. B. R. 113), so that the rule upheld in *Randolph v. Scruggs*, supra, in reference to a voluntary assignment for the benefit of creditors, is equally applicable to this claim. Such claim is allowable only upon equitable considerations for services from which the estate in bankruptcy has derived benefit, and to the extent only that they were beneficial in fact. The rule thus governing the claim was recognized by the District Court in its conclusions, and the order of reversal and its allowance rests primarily on the finding of fact that the services 'were not beneficial to said estate.' Upon the record certified by the referee, and without reference to other matters for the consideration of which error is assigned, we are constrained to the opinion that the services embraced in the claim were so largely directed to delaying and obstructing rightful proceedings in bankruptcy that they cannot be treated as beneficial to the estate, and are without equity for support of the claim to be compensated out of the estate in bankruptcy.

"Institution of the suit against the corporation was plainly within the rights of the plaintiffs therein and their attorneys, the appellants. So the application for and appointment of a receiver to administer the assets and rightful possession thereunder up to the intervention of bankruptcy proceedings are not questionable."

Compare, analogously, In *re Chase*, 10 A. B. R. 683, 124 Fed. 753 (C. C. A. R. I.): "But neither the present statutes of bankruptcy nor any prior act do, or did unqualifiedly denounce an assignment like that at bar, intended for the equal distribution of the property of a failing debtor among creditors, without any attempt to defraud or embarrass persons to whom he is under liability. In this respect, assignments at common law stand precisely as do proceedings for the appointment of receivers by Federal courts or State courts, which, under the act to amend the Act of July 1, 1898, approved February 5, 1903, become a sufficient basis for an involuntary petition. In § 2 of that act (32 Stat. 797, ch. 487), the making a general assignment and an application for a receiver, under the circumstances named therein, are classed together; so that there is nothing in the terms of the present statutes of bankruptcy to justify a claim that an assignment for the benefit of creditors, like that at bar, is any more in fraud of the statutes, or denounced by them, than the action of a State tribunal, which may be one of the highest authority, in proceeding on an honest application for receiver. It can be no more reprehensible to make an assignment in favor of creditors, free from any attempt to embarrass them and from any dishonest purpose, than to apply to a Federal court or State court for the appointment of a receiver; and the bankruptcy statutes do not seek to punish one more than the other."

⁸⁸ In *re Weedman Stave Co.*, 29 A. B. R. 460, 199 Fed. 948 (D. C. Ark.).

Compare, inferentially, In *re Zier & Co.*, 11 A. B. R. 527 (D. C. Ind.).

Compare for case of trusteeship since 1903, but where question not involved. In *re Hercules Atkins Co.*, 13 A. B. R. 39, 133 Fed. 813 (D. C. Penn.).

Conversely, where no benefit resulted therefrom.⁸⁹ Even before the amendment making receiverships acts of bankruptcy was passed, such lien was recognized.⁹⁰

Inferentially, *Wilson v. Parr*, 8 A. B. R. 230, 115 Ga. 629: "The services of the receiver and his attorneys inured to the benefit of the creditors of the bankruptcy. They were rendered under the order of the State court, and the fund in that court was the result of the services of the receiver and his attorneys acting under the orders of the court, and ought to be paid. As this fund in any court would be property chargeable with such costs and expenses, and as the services of both the receiver and the attorneys in the original equitable petition were concluded by the order of transfer, there existed no reason why, before the transfer was made, the expenses of raising the fund transferred should not be paid."

At least wherever the assets already had been converted into money and the court appointing the receiver or trustee had made the allowance before ordering the fund turned over to the bankruptcy court.⁹¹

§ 1617. Likewise, Mortgagees in Possession under Mortgage Executed for Benefit of All Creditors Assenting.—And the same rule would perhaps apply to mortgagees in possession under a mortgage executed for the benefit of all creditors assenting thereto.⁹²

§ 1617½. And Transferees under Arrangements for Effecting Compositions Out of Court.—And doubtless the same rule would apply to agents and transferees under arrangements for effecting compositions with creditors out of court.⁹³

§ 1618. Also, Attaching Creditors Where Attachment Lien Preserved for Benefit of Estate.—It has also been held proper to allow attorney's fees and costs to a creditor who had, prior to bankruptcy, levied an attachment as to which an unfiled or unrecorded instrument was void, the attachment lien being itself void as against the trustee in bankruptcy, but being preserved for the benefit of the estate⁹⁴ in order that the property affected by the unfiled instrument might be brought into the estate.

And the same rule apparently has been held applicable in favor of the

^{89.} In re Allison Lumber Co., 14 A. B. R. 78 (D. C. Ga.); In re Zier & Co., 11 A. B. R. 527 (D. C. Ind.).

^{90.} *Hanson v. Stephens*, 11 A. B. R. 172 (Sup. Ct. Ga.); In re Rogers, 8 A. B. R. 723 (D. C. Ga.). Compare, In re Lengert Wagon Co., 6 A. B. R. 535, 110 Fed. 927 (D. C. N. Y.); *Mauian v. Carpet Lining Co.*, 6 A. B. R. 734 (R. I. Sup. Ct.).

^{91.} *Wilson v. Parr*, 8 A. B. R. 230, 115 Ga. 629 (Sup. Ct. Ga.).

^{92.} In re Hutchinson Co., 14 A. B. R. 518 (Ref. Mich.).

^{93.} Inferentially, In re Hersey, 22 A. B. R. 856, 171 Fed. 998 (D. C. Iowa).

^{94.} *Receivers v. Staake*, 13 A. B. R. 281, 133 Fed. 717 (C. C. A. Va.), affirmed without, however, adverting to this point, sub nom. *First Nat. Bk. v. Staake*, 15 A. B. R. 639, 202 U. S. 141. See ante, § 1490, and post, § 2018.

But a claim for attachment costs where the attachment lien is vacated by the adjudication and not preserved for the benefit of the estate is not a lien upon the property coming into the bankruptcy court nor is it entitled to priority of payment, ante, § 1485.

sheriff where the attachment lien is not preserved.⁹⁵ But such latter holding seems entirely wrong in principle. The sheriff's costs are a debt of the attaching creditor. They are not at all analogous to receivers' or assignees' charges, incurred in equity for the benefit of all. A sheriff's costs on attachment are not in and of themselves a lien on the funds; they are simply part of the attaching creditor's judgment lien. The judgment for costs in attachment is like the rest of the judgment in favor of one party against the other—"and that he do recover his costs herein" is the ordinary formula—and the court officer is not a party and has not an independent lien. His rights rise no higher than those of his principal—the judgment creditor; and there is no reason why one part of the judgment creditor's lien—that for his costs—should be unaffected by the debtor's bankruptcy whilst the rest of it is affected thereby.

§ 1619. Where Attachment Really for Benefit of All, Creditor Entitled to Reimbursement.—Where, however, an attachment suit has in reality been brought for the benefit of all the creditor may be entitled (although not in every State nor in every case) to reimbursement of his costs and expenses. Thus, where the state statute provides for such priority in cases of subsequent sequestrations by receivers, assignees, etc., the same priority may be allowed under § 64 (b) (5).⁹⁶

Again, where property which had been concealed or transferred by the bankrupt, has been recovered through the efforts of the creditor, the creditor may be entitled to reimbursement, under § 64 (b) (2), though such efforts be taken in the form of an attachment, emergency existing.

§ 1620. Whether Extent of Lien May Be Fixed by State Court before Surrender.—It has been held impertinence for the state court to fix the amount of the lien upon the assets in favor of its own officers, at least in state insolvency proceedings suspended by the Bankrupt Act; and that the extent and validity thereof should be left to the bankruptcy court for determination.

Compare, inferentially (only indirectly in point), *In re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio): "The relation of the assignee to the estate of the bankrupt made it manifestly proper that he render his account to the bankruptcy court, and have there determined the questions of his compensation and disbursements in executing the trust."

In re Rogers, 8 A. B. R. 723 (D. C. Ga.): "The trustee either has or has not the right to the possession of the assets of the bankrupt in the hands of the temporary receiver of the State court. * * * If, then, the proceedings are suspended, as is clearly the effect of the bankruptcy law (this being a State insolvency proceeding) the State court has no right or authority to fix the

⁹⁵. *In re Schmidt & Co.*, 21 A. B. R. 593, 165 Fed. 1006 (C. C. A. N. Y.), quoted at § 1486.

⁹⁶. See post, § 2018. *In re Goldberg*, 16 A. B. R. 523, 144 Fed. 566 (D.

C. Me.); *In re Lewes*, 4 A. B. R. 51, 99 Fed. 935 (D. C. Mass.). Obiter, *In re Daniels*, 6 A. B. R. 700, 110 Fed. 745 (D. C. R. I.).

fees of its receiver having charge of the property and less right to refuse to turn over the same until those fees have been paid by the proper officer of the Bankrupt court. * * * Should such a precedent be recognized, it may not be impossible that in a large number of bankruptcy cases the assets might suffer from a mulcting process of this sort before they reach the hands of the officers appointed under the act of Congress to administer and distribute them."

And there is no good reason for applying a different rule where the custody of the state court is under nullified legal liens,⁹⁷ assignments and receiverships, unless perhaps under the doctrine that as to the insolvency proceedings the court was absolutely without jurisdiction in any event, whilst in the other cases the state court's jurisdiction was good until bankruptcy intervened.

It was held not proper for the state court to make the order turning over the assets conditional on the payment of the receivership expenses where the assets had not been converted into money, and that, under such circumstances, the extent and validity of the lien was to be left to the discretion of the bankruptcy court.⁹⁸

Hanson v. Stephens, 11 A. B. R. 172, 116 Ga. 722, wherein the court says: "While a fund raised by the sale of the property of an insolvent debtor, through the medium of a receiver under the orders of a State court, may, on the application of a trustee, appointed after an adjudication of such debtor as a bankrupt, for a transfer of such fund in the State court to him, be charged with the cost and expenses of converting the property of the debtor into cash, yet after the property of a debtor has been seized under the order of a State court and placed in the hands of a temporary receiver, and after the adjudication of such person as a bankrupt, and before the conversion of his property into cash has been made by the receiver, the trustee, on application to the State court, is entitled to the possession of the property for the purpose of being sold and administered in the court of bankruptcy; and it is error on the part of the judge of the State court to order the transfer of such property to the trustee on condition that the fees for the attorneys and receiver shall be first paid.

"Where no fund is in the hands of the receiver, out of which such payments may be made, the persons claiming to be paid out of the property must be remitted to the bankruptcy court for the adjudication and establishment of their respective claims."

Contra, Mauran v. Carpet Lining Co., 6 A. B. R. 734, 23 R. I. 324: "In so doing, however, the question of procedure arises, whether the expenses already incurred shall be first paid out of the fund, or whether the whole fund shall be surrendered and our receiver sent to the Federal court to ask for his fees and expenses. We think that the former is the proper course for several reasons.

"A receiver is an officer of the court, holding property under its order for the benefit of the party entitled to it. All courts therefore hold that the receiver should be paid from the fund, as a part of the expenses of the proceeding. It would greatly embarrass courts in securing good receivers if this rule should not be adhered to. They should not be subjected to the uncertainty, inconvenience and delay of awaiting other proceedings and of seeking their pay from other courts."

⁹⁷. Instance, *In re Hecox*, 21 A. B. R. 314, 164 Fed. 823 (C. C. A. Colo.).

⁹⁸. *Contra, Wilson v. Parr*, 8 A. B. R. 230, 115 Ga. 629.

It has also been held improper for the state court to order the sale of the assets for the purpose of raising the money to pay such charges.

But at all events, in cases where the assets were in the State bankruptcy or insolvency court, the extent and validity of the lien must be left to the United States bankruptcy court for determination;¹ and it will be considered an impropriety, which may be disregarded, for the state court to attempt to fix them.²

And yet as to receiverships and assignments superseded by bankruptcy, at any rate, the rule seems to be that it is not improper for the State court to settle its receiver's or assignee's account before turning over the assets.³

Obiter, *In re Watts and Sachs*, 190 U. S. 1, 35, 10 A. B. R. 113: “* * * but it remained for the State court to transfer the assets, settle the accounts of its receiver, and close its connection with the matter. Errors, if any, committed in so doing could be rectified in due course and in the designated way.”

But at any rate if the State court receiver voluntarily turns over the property to the bankrupts, under order of the State court, and then the bankruptcy court takes possession, the State court has lost jurisdiction to determine allowances to its receiver, even though the State court had obtained possession originally more than four months before the bankruptcy.

In re Rogers & Stefani, 19 A. B. R. 566, 156 Fed. 267 (D. C. Ark.): “This case, therefore, stands in this attitude, the State court, by its own orders, caused its receiver to surrender the bankrupts' estate to the bankrupts, in whose possession it was subsequently seized by the trustee in bankruptcy. Afterwards that court made an order fixing the allowance of its receiver, his attorney, and its clerk, and made such allowance a preferred claim upon the assets of the bankrupt in the hands of the trustee, and caused the same to be certified to the Bankrupt Court accordingly. In effect the making of his order was tantamount to an effort on the part of the State court to administer, as far as this order went, the estate of the bankrupt, rightfully and previously in the possession of the bankrupt court.”

The statutory rate of compensation under the State law cannot be considered binding upon the Bankruptcy Court.

In re Hays, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio): “The referee took the view, and we think correctly, that the right to commissions under the Ohio Statute, rather than under the Bankruptcy Act, was not a matter of fixed legal right, inasmuch as the assignment had never been completed and had in fact existed but a short time previous to the institution of the bankruptcy proceedings.”

1. *In re Rogers*, 8 A. B. R. 723, 116 Fed. 435 (D. C. Ga.); *In re Allison Lumber Co.*, 14 A. B. R. 78 (D. C. Ga.).

2. *In re Rogers*, 8 A. B. R. 723, 116 Fed. 435 (D. C. Ga.).

3. Obiter, *Loveless v. Southern Grocer Co.*, 20 A. B. R. 180, 159 Fed. 415 (C. C. A. La.), quoted at § 1611½;

also, see post, §§ 1838, 1839, et seq.; also, see obiter, *In re Rogers & Stefani*, 19 A. B. R. 566, 156 Fed. 267 (D. C. Ark.); but compare, apparently contra, *In re Hecox*, 21 A. B. R. 314, 164 Fed. 823 (C. C. A. Colo.), quoted, on other points, at § 1611.

§ 1621. Only Expenses and Compensation for Services Beneficial to Estate and Reasonable, Allowed.—Only such expenses and compensation as were incurred, or earned, in performing services beneficial to the estate or necessary to its preservation, and that are reasonable in amount, may be allowed as part of the lien.⁴

Randolph v. Scruggs, 190 U. S. 533, 10 A. B. R. 1: "We are not prepared to go further than to allow compensation for services which were beneficial to the estate. Beyond that point, we must throw the risk of his conduct on the assignee, as he was chargeable with knowledge of what might happen."

In *re Chase*, 10 A. B. R. 683, 124 Fed. 753 (C. C. A. R. I.): "From the time the assignor declares his insolvency by making an assignment, his property must be held equitably for the benefit of his creditors, and he can do nothing which will embarrass or prejudice them in realizing therefrom, whether the result is that they are administered under the common law assignment or ultimately go into the hands of a trustee in bankruptcy. Therefore, in no event can he impress on them a lien for any amount of compensation arbitrarily agreed on. Anything in this direction beyond what would be reasonable and equitable would be contrary to the policy of the law, and would be declared invalid by the court having jurisdiction of the trust if the assignment is worked out at common law, or by the court in bankruptcy if the property finally comes under its control. * * *

"Therefore, in the present case, the District Court should ascertain and determine whether, under all the circumstances, the petitioners are equitably entitled to their disbursements, or any part thereof, reasonable allowances for their services, and protection against outstanding claims for rent."

Thus, attorney's services to an assignee that are beneficial to the estate, rendered before the adjudication in bankruptcy, may form part of the assignee's lien upon the assets turned over, where the assignment itself provides for priority of expenses out of the assigned property.⁵ And an attorney who represents certain creditors, or their agents, in an attempt to administer the debtor's assets so as to avoid bankruptcy proceedings, may be entitled to compensation; and the creditors, or their agents, may be allowed therefor on accounting to the estate, should the debtor be subsequently adjudged bankrupt.⁶

But attorney's services in preparing the deed of assignment are not entitled to a place in the lien upon the assets thus turned over;⁷ though they may be proved as a general claim against the bankrupt's estate.⁸ Nor

4. In *re Zier & Co.*, 15 A. B. R. 648, 142 Fed. 102 (C. C. A. Ind., affirming 11 A. B. R. 527), quoted *supra*, § 1616; impliedly, In *re Allison Lumber Co.*, 14 A. B. R. 78, 137 Fed. 643 (D. C. Ga.). Compare, In *re Rogers & Stefani*, 19 A. B. R. 566, 156 Fed. 267 (D. C. Ark.).

In *re Standard, etc., Co.*, 26 A. B. R. 562, 186 Fed. 578 (D. C. Ala.); impliedly, In *re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio), quoted *post* in this same section, § 1621. Compare *Eichholz v. Polack*, 25 A. B. R.

243, 140 App. Div. N. Y. 551, where allowances for expense were claimed by an assignee for particular creditors.

5. *Randolph v. Scruggs*, 190 U. S. 533; S. C., 10 A. B. R. 1; In *re Byerly*, 12 A. B. R. 186, 128 Fed. 637 (D. C. Penn.).

6. In *re Marble Products Co.*, 29 A. B. R. 384, 199 Fed. 668 (D. C. N. Y.).

7. *Randolph v. Scruggs*, 190 U. S. 533; S. C., 10 A. B. R. 1.

8. *Randolph v. Scruggs*, 190 U. S. 533; S. C., 10 A. B. R. 1.

may attorney's services rendered the assignee or assignor in resisting adjudication of bankruptcy be allowed.⁹

In *re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio): "The referee took that the assignee has no lien upon the funds by way of a preferred claim for expenses for resisting this adjudication." Quoted further at § 1621 and § 1665.

Nor attorney's services rendered the debtor or the receiver in the State court in avoiding bankruptcy proceedings, really in behalf of preferred creditors, although ostensibly for the debtor, or in resisting adjudication in bankruptcy.

In *re Zier & Co.*, 11 A. B. R. 527 (D. C. Ind., affirmed 15 A. B. R. 648): "The reason of this rule is that general creditors should pay for services which have actually benefited them. It was never intended to make them pay for unsuccessful assaults upon their interests as well as resistance to those assaults. The suit in the Floyd Circuit Court was collusive and fraudulent. It was fraudulent as against general creditors in bankruptcy, because it permitted the manager of an insolvent corporation to take from its assets a sum equal to one-third of them, and to apply that sum upon the claims of particular creditors. Its natural and inevitable result was to uphold and protect fraudulent preferences, while the bankruptcy proceedings were in the interest of all the creditors alike. Watts, as attorney for the receiver of the Floyd Circuit Court, aided in every possible way in the promotion of this result."

In *re Zier & Co.*, 15 A. B. R. 648, 142 Fed. 102 (affirming 11 A. B. R. 527): "Nor is it material to the present issue that the Supreme Court (*In re Watts and Sachs*, *supra*) held that these parties 'entertained the conviction in good faith that the custody of the State court could not be lawfully interfered with by the bankruptcy court,' and were acting erroneously, but not in contempt of the District Court, and so discharged them from the adjudication of that court for contempt. The services of the appellants were persistent in obstructing both resort to and proceedings in bankruptcy, and caused injury and expense to the estate which were unaffected by their motives; so that their incidental service in making sundry collections and negotiating settlements is not entitled to independent recognition for allowance."

But allowance may be made for services and for reimbursement of expenses occurring *after* the filing of the bankruptcy petition as well as before, if the assignee remains in possession.

In *re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio): "We think it clear the view that under the decision in *Randolph v. Scruggs*, 190 U. S. 533, 10 Am. B. R. 1, 23 Sup. Ct. 710, 47 L. Ed. 1165, the assignee was entitled to compensation for such services and disbursements as he had made which benefited the estate. In view of the relations of the assignee to the estate subsequent to the filing of the petition in bankruptcy, he included in the same rule the services and disbursements up to the time of the appointment of the trustee in bankruptcy. In our opinion the referee took the right view. It is true that after the filing of the petition in bankruptcy the assignee took the risk of having his proceedings under the assignment set aside, but as no application for receivership was made, the assignee may not improperly be treated (with respect to the settlement of his

9. *Randolph v. Scruggs*, 190 U. S. 533; S. C., 10 A. B. R. 1.

accounts) as a quasi receiver during the pendency of the proceedings for adjudication in bankruptcy."

§ 1622. Others' Rights to Be Worked Out Through Assignee or Receiver.—And the rights of the assignee's attorney and others serving the assignee or receiver, in the bankrupt fund are to be worked out through the assignee or receiver, and by virtue of the latter's lien; and such attorney or other person has no independent standing in the bankruptcy court.¹⁰

Randolph v. Scruggs, 190 U. S. 533, 10 A. B. R. 1: "The more difficult question is how to deal with the services rendered to the voluntary assignee. The claim for them must be worked out through the assignee, and cannot be put higher than his claim for allowance, supposing that they had been paid."

In *re Byerly*, 12 A. B. R. 186, 128 Fed. 637 (D. C. Pa.): "As pointed out in *Randolph v. Scruggs*, the claim as is now presented must be worked out through the accountant in his former capacity as assignee and cannot be put any higher than an allowance to him, for necessary counsel fees paid."

Thus, the attorney may not except to the referee's ruling thereon nor prosecute error nor appeal.¹¹ So, also, must be worked out the rights of parties furnishing material to the state receiver; and lienholders thereon will have no rights in the bankruptcy court unless the property can be shown to have come into the custody of that court.¹²

§ 1623. How Assignee's or Receiver's Rights to Be Presented.—The assignee or receiver in the State court should present his claim to the bankruptcy court by way of a petition, or perhaps deposition for proof of a secured debt, like any other party claiming a lien on a fund in the custody of the bankruptcy court.¹³

And where the assignee submits his account to a court of bankruptcy for judicial examination, he will be bound by its determination.¹⁴

§ 1623½. Adverse Claimant's Rights Preserved.—Properly, the order of surrender should provide that the turning over of the property should be subject to the rights of adverse claimants and others; although the failure of the order to specifically so provide could not prejudice the claimant's rights.

Thus, where the trustee in bankruptcy makes distribution of the property, or turns it back to the bankrupt on confirmation of a composition, without having the court first pass upon an adverse claimant's rights, the trustee may be held, in proper cases, personally liable to such adverse claimant.¹⁵

10. In *re Standard, etc., Co.*, 26 A. B. R. 562, 186 Fed. 578 (D. C. Ala.).

11. In *re Byerly*, 12 A. B. R. 186, 128 Fed. 637 (D. C. Penn.).

12. In *re Allison Lumber Co.*, 14 A. B. R. 78 (D. C. Ga.).

13. In *re Allison Lumber Co.*, 14 A. B. R. 78 (D. C. Ga.).

14. In *re Manzai Mfg. Co.*, 25 A. B. R. 497, 183 Fed. 298 (C. C. A. N. Y.).

15. In *re Cadenas & Coe*, 24 A. B. R. 135, 178 Fed. 158 (D. C. N. Y.), quoted at § 2398.

§ 1624. Liability on Assignee's Bond on Superseding of State Court's Custody.—The trustee may maintain an action upon the assignee's bond [on leave of the State court, in New York], to recover the amount which the assignee fails to turn over to the trustee.¹⁶

And the finding of the bankruptcy court, as to the amount to be surrendered by the assignee, where made on proper notice and hearing as to funds still in the assignee's hands, or voluntarily accounted for by him, may be the basis for the suit on the bond.¹⁷

However, the surety upon the assignee's bond will not be bound by the bankruptcy court's order of accounting, where such surety has not been notified nor allowed to defend.¹⁹

DIVISION 3.

STATE BANKRUPTCY OR INSOLVENCY PROCEEDINGS SUPERSEDED BY BANKRUPTCY.

§ 1625. Third Exception to Rule That State Court Retains Jurisdiction if First to Obtain Custody.—The third exception to the rule that the State court retains jurisdiction if first in possession of the res, is where the property at the time of the bankruptcy is in the custody of a State court under state insolvency or state bankruptcy proceedings, or proceedings amounting to such, in which event such proceedings are superseded by the federal bankruptcy proceedings.²⁰

In re Kersten, 6 A. B. R. 519, 110 Fed. 929 (D. C. Wis.): "It is true that jurisdiction over the estate of a bankrupt is essential for its due administration under the provisions of the Act of Congress. * * * The showing in this record of the action pending in the Circuit Court of Calumet County, and of its custody of the estate, through a receiver, under the provisions of the State

16. Brandt on Suretyship, § 128. Cohen v. American Surety Co., 20 A. B. R. 65, 192 N. Y. App. 227, affirming 19 A. B. R. 901, 123 App. Div. 519, 108 N. Y. Supp. 519. Apparently assuming that the bond is liable for proper turning over of assets, whether to State court or to trustee in bankruptcy. Cohen v. Am. Surety Co., 22 A. B. R. 909, 132 App. Div. (N. Y.) 917.

17. Cohen v. American Surety Co., 20 A. B. R. 65 (N. Y. App.), affirming 19 A. B. R. 901, 123 App. Div. 519, 108 N. Y. Supp. 519.

19. Cohen v. Am. Surety Co., 22 A. B. R. 909, 132 App. Div. (N. Y.) 917.

20. Mauran v. Carpet Lining Co., 6 A. B. R. 734 (R. I. Sup. Ct.); In re Storck Lbr. Co., 8 A. B. R. 86, 114 Fed. 860 (D. C. Md.); In re Smith & Dodson, 2 A. B. R. 9 (D. C. Ind.); Herron Co. v. Superior Court, 8 A. B.

R. 493 (Sup. Ct. Calif.); Wescott v. Berry, 4 A. B. R. 265, 45 Atl. 352 (Sup. Ct. N. H.); Carling v. Seymour Lbr. Co., 8 A. B. R. 26, 113 Fed. 483 (C. C. A. Ga., reversing In re Macon Lbr. Co., 7 A. B. R. 66); Ketcham v. McNamara, 6 A. B. R. 163, 72 Conn. 709; Parmenter Mfg. Co. v. Hamilton, 1 A. B. R. 41 (D. C. Mass.); In re Bruss-Ritter Co., 1 A. B. R. 59, 90 Fed. 651 (D. C. Wis.); In re Etheridge, 1 A. B. R. 115, 92 Fed. 329 (D. C. Ky.); In re McKee, 1 A. B. R. 311 (D. C. Ky.); Littlefield v. Gray, 8 A. B. R. 409, 52 Atl. 925 (Me.); In re F. A. Hall Co., 10 A. B. R. 96 (D. C. Conn.); In re Curtis, 1 A. B. R. 440, 91 Fed. 737 (D. C. Ills.); Singer v. Nat'l Bedstead Mfg. Co., 11 A. B. R. 276 (N. J. Ch.); Old Town Bank v. McCormick, 10 A. B. R. 768, 96 Md. 341; obiter, In re Salmon & Salmon, 16 A. B. R. 131, 143 Fed. 395 (D. C. Mo.).

statute. * * * If such action involves administration of the estates of debtors within the statute, in the nature of insolvency proceedings it cannot be doubted that jurisdiction to that end is suspended when an adjudication of bankruptcy intervenes and becomes paramount under the Bankruptcy Act adopted by Congress in conformity to the powers reserved in the constitution."

In *re* Lengert Wagon Co., 6 A. B. R. 535, 110 Fed. 927 (D. C. N. Y.): "But the proceedings in the State Court is one incident to the insolvency of the corporation, and it seems to be well settled that the Bankruptcy Act gives exclusive jurisdiction to the United States courts in such matters, where proceedings are properly instituted, and ousts the State courts of all jurisdiction with respect to the possession or distribution of insolvent estates."

Inferentially, In *re* Watts, 190 U. S. 1, 10 A. B. R. 113: "And the operation of the bankruptcy laws of the United States cannot be defeated by insolvent commercial corporations applying to be wound up under State Statutes. The Bankruptcy Law is paramount, and the jurisdiction of the Federal courts in bankruptcy, when properly invoked, in the administration of the affairs of insolvent persons and corporations, is essentially exclusive. Necessarily when like proceedings in the State courts are determined by the commencement of proceedings in bankruptcy, care has to be taken to avoid collision in respect of property in possession of the state courts. Such cases are not cases of adverse possession or of possession in enforcement of pre-existing liens, or in aid of the bankruptcy proceedings. The general rule as between courts of concurrent jurisdiction is that property already in possession of the receiver of one court cannot rightfully be taken from him without the court's consent, by the receiver of another court appointed, in a subsequent suit, but that rule can have only a qualified application where winding up proceedings are superseded by those in bankruptcy as to which the jurisdiction is not concurrent."

Potts v. Smith Mfg. Co., 12 A. B. R. 392, 25 Pa. Superior Ct. 209: "The Pennsylvania Act of June 4, 1901, relating to insolvency is suspended by reason of the existence of the Federal Bankrupt Act of July 1, 1898, and does not become operative as to the persons and subjects to which the Federal act applies."

§ 1626. Basis of Supersedence, Paramount Authority Conferred by Constitution, and Necessary Implication from § 70.—The superseding of State Bankruptcy and State Insolvency proceedings comes about from the fact that the Constitution of the United States in Article 1, § 8, authorizes Congress "to establish * * * uniform laws on the subject of bankruptcies throughout the United States;"²¹ and that § 71 of the original Act [since stricken out on Amendment], providing that "Proceedings commenced under State Insolvency laws before the passage of this Act shall not be affected by it," necessarily implies the superseding of all other classes of State insolvency proceedings than those expressly excepted.

Potts v. Smith Mfg. Co., 12 A. B. R. 392, 25 Pa. Super. Ct. 209: "The Federal Courts have applied this rule to the subject of bankruptcies, and have held that

²¹ In *re* Storck Lumber Co., 8 A. B. R. 86, 114 Fed. 860 (D. C. Md.); In *re* Watts, 10 A. B. R. 113, 190 U. S. 1; In *re* Bruss-Ritter Co., 1 A. B. R. 59, 90 Fed. 651 (D. C. Wis.); In *re* Etheridge Furn. Co., 1 A. B. R. 115, 92 Fed. 329 (D. C. Ky.); In *re* McKee, 1 A. B. R. 313 (D. C. Ky.).

when Congress has legislated upon the subject by the enactment of a bankrupt law the power of the States is controlled and suspended."

Mauran v. Carpet Lining Co., 6 A. B. R. 737, 23 R. I. 324: "The plenary and paramount power of Congress to establish uniform laws on the subject of bankruptcies throughout the United States,' says Hall, J., in *In re Deposit and Savings Inst.*, Fed. Cas., No. 12, 211, p. 141, 'is given in express terms by the Constitution of the United States. It is therefore very clear that when Congress has exercised the power thus conferred their action must necessarily control or limit the exercise of the power of the States over the same subject matter; and that whenever any State legislation, or any action of the State courts, comes practically into actual conflict with the proper execution of the laws of Congress, constitutionally passed under such grant of power, State legislation and the jurisdiction and action of the State courts must yield to the paramount authority of the national government.'

"The object and intent of the national bankruptcy law is to place the administration of the affairs of insolvent persons and corporations exclusively under the jurisdiction of the Federal courts sitting as courts of bankruptcy; and the enactment of the national bankrupt law now in force suspended all action and proceedings under State insolvent laws not commenced before the passage of the national Bankruptcy Act, at least in all cases provided for by such Bankruptcy Act. In *re Merchants' Ins. Co.*, 3 Biss. 162, 6 Nat. Bankr. Reg. 43, Fed. Cas. No. 9, 441; U. S. Bankruptcy Act, § 70, last clause."

Herron Co. v. Superior Ct., 8 A. B. R. 493, 136 Calif. 279: "The provisions in the Constitution of the United States conferring upon Congress the power 'to establish uniform laws on the subject of bankruptcies throughout the United States,' of necessity makes any act of Congress pass upon that subject the supreme law of the land, and it was at a very early day determined that the effect of such action of Congress is to suspend and supersede the operation of any State law of insolvency whenever there is any conflict between the two. There can be no concurrent jurisdiction in the two sovereignties over the same subject, and, as the people of the several States have yielded to the United States the power to enact laws upon this subject, it follows that when the United States has enacted a law the power of the State to enforce its own law upon that subject, whether it be similar or different, must yield to what is the supreme law of the land."

Wescott v. Berry, 4 A. B. R. 265, 45 Atl. 352 (Sup. Ct. N. H.): "The power of the several States to enact insolvency laws is subject to the power of Congress to establish 'uniform laws on the subject of bankruptcies throughout the United States.' Accordingly a general bankruptcy act suspends State insolvency laws from the time it goes into effect. * * * The provisions that 'proceedings commenced under State insolvency laws before the passage of this act shall not be affected by it' seems conclusive evidence that this was not the intention of Congress; for the provision that this act shall not affect proceedings begun under the State law before its passage necessarily implies that no proceedings can be brought under State insolvency laws after that date."

Carling v. Seymour Lumber Co., 8 A. B. R. 36, 113 Fed. 483 (C. C. A. Ga., reversing *In re Macon Lbr. Co.*, 7 A. B. R. 66): "The Constitution limits the power of a State to legislate on this subject, for it is not permitted to so legislate as to impair the obligation of contracts. U. S. Const., art. I, § 10. This act is clearly a State insolvency law, within the power of the State to enact when the Congress has not exercised its power to pass a uniform bankrupt law. The administration of the estates of insolvents by the State courts under this statute would be inconsistent with the exclusive jurisdiction of the courts of bankruptcy under the bankrupt law. The passage of the bankrupt law by

Congress, therefore suspended the operation of the State statute. *Sturges v. Crowninshield*, 4 Wheat. 122-186; *Tua v. Carriere*, 117 U. S. 201-210; *Butler v. Gorely*, 146 U. S. 303-314."

Ketcham v. McNamara, 6 A. B. R. 163, 72 Conn. 709: "The Constitution of the United States gives Congress power to establish uniform laws on the subject of bankruptcies throughout the United States. At the date of the assignment to the plaintiff such laws had been established. They covered, so far as respects the rights of the parties to the case at bar, the same field previously occupied by the insolvent laws of this State, and consequently they superseded them. * * *

"The Act of 1898 also differs from that of 1867 in that it makes direct reference to its effect upon State insolvent laws. Its concluding provision is that 'proceedings commenced under State insolvency laws before the passage of this act shall not be affected by it.' The necessary implication is that any such proceedings commenced after the passage of the act are affected by it."

Parmenter Mfg. Co. v. Hamilton, 1 A. B. R. 41, 172 Mass. 178: "The only saving clause affecting the jurisdiction of the State Courts provides for cases commenced in those courts before the passage of the act.

"The plain implication is that proceedings commenced in the State court after the passage of the act are unauthorized. This is in accordance with the earlier language giving the statute full force and effect from the time of its passage, except that the filing of petitions is to be postponed for a short time.

"We are of opinion that the language was chosen to make clear the purpose of Congress that the new system of bankruptcy should supersede all State laws in regard to insolvency from the date of the passage of the statute."

§ 1627. State Bankruptcy and Insolvency Laws Not Prohibited.

—This constitutional provision does not prohibit the states enacting State bankruptcy laws.²²

Sturges v. Crowninshield, 4 Wheat. (U. S.) 122: "This establishment of uniformity is perhaps incompatible with State legislation on that part of the subject to which the act of Congress may extend. * * * It does not appear to be a violent construction of the constitution, and is certainly a convenient one, to consider the power of the States, as existing over such cases as the laws of the Union may not reach; but, be this as it may, the power granted to Congress may be exercised or declined, as the wisdom of that body shall decide. If, in the opinion of Congress uniform laws concerning bankruptcies ought not to be established, it does not follow that partial laws may not exist, or that State legislation on the subject must cease. It is not the mere existence of the power, but its exercise, which is incompatible with the exercise of the same power by the States. It is not the right to establish these uniform laws, but their actual establishment, which is inconsistent with the partial acts of the States."

Potts v. Smith Mfg. Co., 12 A. B. R. 392, 25 Pa. Super. Ct. 209: "It is not contended that the power vested in Congress by the Constitution of the United States is exclusive of that of the States, and that there remains no power in the latter to legislate upon the subject. It is an established doctrine that the powers granted to Congress are only exclusive of the powers upon the same subject existing in the States when an exclusive power is expressly delegated to Congress, or there is such incompatibility in the exercise of it by the States

²² *Herron Co. v. Superior Ct.*, 8 A. Bk. *v. McCormick*, 10 A. B. R. 768, 96 B. R. 493 (Sup. Ct. Calif.); *Oldtown Md.* 341.

as to produce the necessary conclusion that it is exclusive in Congress. Where there is no such exclusive grant to Congress, of such incompatibility, concurrent power remains with the States. Where, however, in the case of concurrent powers Congress has exercised its powers on a given subject, the control of the State over that subject is by such action of Congress prohibited. 1 Kent's Com. 390."

Singer v. Nat. Bedstead Co., 11 A. B. R. 27 (N. J. Ch.): "A more or less indefinite, and I think misleading, notion has sometimes been expressed that the Constitution has committed to Congress the whole subject of bankruptcy and insolvency for appropriate legislation, and that therefore whenever Congress passes a general bankrupt law, which it has done four times, each time naming, it a 'uniform system of bankruptcy,' all power on the part of the States to legislate upon the subject of bankruptcy or insolvency is immediately suspended. The premise may be deemed to be correct, but it seems to me that the conclusion is entirely erroneous. Congress is not obliged to legislate on the whole subject of bankruptcy, it may deal with only one or several parts. It is the enactment by Congress of a law applicable to a particular case which suspends any State law which otherwise would be applicable to that case. If every case of bankruptcy or insolvency were within the operation of a National Bankrupt Act, then no possible State law on the subject of bankruptcy or insolvency would have any vigor, but every such law would ipso facto be suspended." Quoted further at § 1628.

Analogously, *In re Milling Co.*, 16 A. B. R. 455, 457, 144 Fed. 314 (D. C. Tex.): "The prohibition against impairing the obligation of contracts * * * is directed against the States only, and there is no other clause in the constitution laying a like inhibition upon Congress."

Some of the states have very complete bankruptcy laws providing for both involuntary and voluntary proceedings, as for instance, Massachusetts, whose law is called an insolvency law, yet possesses all the distinguishing features of a true bankruptcy law, even to the discharge of debtors from the remainder of their debts. So, also, with the following states: Maine, New Hampshire, Vermont, Connecticut, Rhode Island, California, Georgia, Louisiana, Maryland, Minnesota, Nevada, Pennsylvania^{22a} and North Dakota. But as to Pennsylvania, one case holds contra.²³

The following States have provisions for assignments, or for the discharge of the debtor, but not for involuntary proceedings: New Jersey, North Carolina, Oregon, Virginia, Washington, Wisconsin, Wyoming.

It naturally occurs to the mind that for a state to pass a law discharging a debtor from his debts would contravene § 10 of the same Article of the United States Constitution, providing that "no State shall * * * pass any law impairing the obligation of contracts;" and, in truth, so would such law, were it made to apply to obligations arising outside the boundaries of the state or arising before the law was passed. But these state insolvency laws discharging debtors from their obligations uniformly have been held not to be retroactive and to be applicable only to debts contracted within the state after their enactment; and thus, under the familiar rule that

^{22a}. *Potts v. Smith Mfg. Co.*, 12 A. B. R. 392, 25 Pa. Super. Court 205.

²³. *In re Crawford*, 18 A. B. R. 618, 154 Fed. 769 (C. C. A. Pa.).

an existing statute is to be read into every contract as a part of its terms the same as if expressly written into it, the courts have held such discharges do not impair the obligation of contracts made within the state after the law has been enacted. It was impliedly part of the very contract itself that its obligations should be liable to be discharged in the event that the debtor was adjudged insolvent.²⁴

But these state insolvency laws discharging debtors from their obligations uniformly have been held to be applicable only to debts contracted within the state.

Baldwin v. Hale, 1 Wall. 223: "Insolvent laws of one State cannot discharge the contracts of citizens of other States, because they have no extraterritorial operation, and consequently the tribunal sitting under them, unless in cases where a citizen of such other State voluntarily becomes a party to the proceeding, has no jurisdiction in the case. Legal notice cannot be given, and consequently there can be no obligation to appear, and of course there can be no legal default. The judgment of the Circuit Court is therefore affirmed with costs."

Smith v. Parsons, 1 Ohio 236: "State insolvent laws discharging debtors from their debts upon surrendering up all their property are valid as to contracts made between citizens of the same state, within its jurisdiction, after the law is enacted."

Analogously, *In re Milling Co.*, 16 A. B. R. 454, 457, 144 Fed. 314 (D. C. Tex.): "The Bankruptcy Act which was of force at the time of the execution of the two notes in question, entered into and formed part of the contract of the parties as if it had been expressly referred to or incorporated in its terms."

As to debts owed outside the state, the creditor is usually required to consent to the proceedings before he will be allowed to share in the dividends. Perhaps, indeed, it is held that he waives his constitutional right to object to a discharge of his claim against the debtor, by merely proving his claim in the proceedings. However that may be, state bankruptcy laws are legal and are on the statute books of many of the states.²⁵

§ 1628. But Suspended during Existence of Federal Bankruptcy Law, as to All Classes Subjected to Latter.—But whenever Congress does pass a bankruptcy law, the law supersedes, as long as it is in existence, all state insolvency or bankruptcy laws relative to persons and acts declared therein to be subjects of bankruptcy; and proceedings under the state insolvency laws regarding debtors who could, upon the doing of the particular act complained of, be subjected to the operation of the federal bankruptcy law are absolutely void, whether or not federal bankruptcy proceedings actually follow; the constitutional provision making the law passed in pursuance of it paramount.²⁶

^{24.} *Baldwin v. Hale*, 1 Wallace 223 (U. S. Sup. Ct.); *Pullen v. Hillman*, 84 Me. 129. Also, see *Lowenberg v. Levine*, 93 Calif. 215. Also, see *obiter*, *Grensfeld Bros. v. Brownell*, 11 A. B. R. 603 (Sup. Ct. N. Mex.).

^{25.} *Brown v. Smart*, 145 U. S. 457; *Denny v. Bennett*, 128 U. S. 498.

^{26.} *Littlefield v. Gray*, 8 A. B. R. 409, 52 Atl. 925 (Me. Sup. Jud. Ct.), quoted post, § 1630. *Herron Co. v. Superior Court*, 8 A. B. R. 493 (Sup.

In re Yoke Vitrified Brick Co., 25 A. B. R. 18, 180 Fed. 235 (D. C. Kan.): " * * * whether that act (state act) shall be construed to give the wage earner priority of payment over fixed liens on the property in the hands of the receiver or assignee remains to be determined. However, as it obviously must be classed among the insolvency laws of the State, its operation remains suspended as to any matter over which a court of bankruptcy has jurisdiction except in so far as the Bankruptcy Act preserves and enforces such act."

Few of the cases state the complete rule as thus given, and it will be necessary to consider the different modified forms of the rule as the various decisions give them.

Singer v. Nat'l Bedstead Co., 11 A. B. R. 279 (N. J. Ch.): "As I read the present Bankrupt Act, the intention of Congress is that every case of bankruptcy or insolvency of which the bankrupt court has jurisdiction is to be dealt with exclusively by that court. The intention of the act is to supply the law of certain cases, and to supply a special court to enforce that law. All other cases of bankruptcy or insolvency are left to be dealt with as the State Legislature may see fit. * * *

"It may be conceded that Congress can provide a law for only a limited number of cases of bankruptcy and insolvency and expressly prohibit the enactment of any other bankrupt or insolvent laws by the States. For present purposes the concession may be that Congress might pass a voluntary system of bankruptcy, and enact that there should be no other law on the subject of bankruptcy or insolvency, voluntary or involuntary, throughout the United States. Even if this be a sound view, it need not be considered, because the present Bankrupt Act contains no words prohibiting States from passing insolvent or bankrupt laws which deal with cases which are not within the operation of the National Bankrupt Act—which are expressly excluded from it. It would be a singular result, indeed, if because Congress has not seen fit to provide a bankrupt law applicable to corporations engaged in operating railroads, steamboats, insurance companies, laundries, livery stables and large numbers of other business enterprises, the inference must be drawn that Congress did not intend that any bankrupt or insolvent laws should be applied to this class of corporations, but that State insolvency laws applicable to them should be suspended.

"So, also, where the corporation might be within the operation of the Federal Bankrupt Act, if it had committed an act of bankruptcy, it remains, it seems to me, without the scope of that act, and within the full operation of State acts in respect of a charge of insolvency which includes no act of bankruptcy as defined by the Bankrupt Act.

"Of course, as I have intimated, it may be admitted that Congress has the

Ct. Calif.), quoted ante, § 1626, and post, § 1630. *Potts v. Smith Mfg. Co.*, 12 A. B. R. 392, 25 Penn. Superior Ct. 209, quoted ante, §§ 1625, 1626, and post, § 1629. *Wescott Co. v. Berry*, 4 A. B. R. 265, 45 Atl. 352 (Sup. Ct. N. H.), quoted ante, § 1626. *Carling v. Seymour Lbr. Co.*, 8 A. B. R. 36, 113 Fed. 482 (C. C. A. Ga., reversing *In re Macon Lumber Co.*, 7 A. B. R. 66), quoted post, §§ 1633 and 1636. *Ketcham v. McNamara*, 6 A. B. R. 160, 72 Conn. 709, quoted ante, §§ 1626 and

1603. *In re C. D. Adams*, 1 A. B. R. 94 (Ref. N. Y.) *In re Etheridge Furn. Co.*, 1 A. B. R. 112, 92 Fed. 329 (D. C. Ky.); *In re Curtis*, 1 A. B. R. 440, 91 Fed. 737 (D. C. Ills.), quoted ante, § 1603. Inferentially, *In re Wright*, 2 A. B. R. 592, 95 Fed. 807 (D. C. Mass.); (1841) *Ex parte Eames*, 2 Story 322. 325, Fed. Cas. 4,237; obiter, *Johnson v. Crawford*, 18 A. B. R. 608, 154 Fed. 761 (D. C. Pa., affirmed sub nom. *In re Crawford*, 18 A. B. R. 618, 154 Fed. 769, C. C. A.).

power to say in the Bankrupt Act that no natural person or corporation, subject to its provisions, shall be liable to be involuntarily deprived of his or its property because of insolvency, at the instance of his or its creditors, under any State statute or in any State court. Congress, however, has said nothing of this kind, nor do I think can such an intention be gathered in any way from any or all of the provisions of the Bankrupt Act. * * *

[Here follows the part quoted, ante, at § 1627.]

"When the present Bankruptcy Act was under discussion in Congress, my recollection is that a large and influential body of our national legislators earnestly proposed to enact merely a voluntary law—a law under which debtors could come into a bankrupt court, lay down their assets and get a discharge. Would anybody seriously argue that if such a 'uniform system of bankruptcy' had been enacted by Congress it would have had the effect to suspend the operation of State bankruptcy and insolvent laws under which insolvent debtors or fraudulent insolvent debtors are brought involuntarily into court and stripped of their assets for the benefit of their creditors?

"The present 'system of bankruptcy,' which Congress saw fit to enact in 1898, does not pretend to cover the whole field of either voluntary or involuntary bankruptcy and insolvency. Corporations are not allowed to become voluntary bankrupts. [Since changed by Amendment of 1910.] Large classes of natural persons and corporations are excluded absolutely from the operation of the involuntary system. All corporations as well as natural persons are excluded if their debts do not amount to \$1,000. It would be a most extraordinary state of affairs if transportation companies, insurance companies and many other kinds of business corporations not within the classes enumerated in the present Bankrupt Act, and also manufacturing, mercantile and trading corporations whose debts do not amount to \$1,000, could not be subjected to the operation of our New Jersey statute, which provides a means for winding them up and distributing their assets. The result would be that such corporations, when insolvent, could not be wound up at all at the instance of their creditors. The Bankrupt Act, § 4 (b), expressly provides that national banks and banks incorporated under State or Federal laws shall not be adjudged involuntary bankrupts, the intention plainly being to leave these respective banking corporations to be wound up under national or State statutes particularly applicable to them.

"It is perfectly plain that State systems of voluntary and involuntary bankruptcy may remain today in full operation upon large numbers of insolvent natural persons and corporations who cannot be brought within the operations of the National Bankrupt Act under any possible state of facts.

"It is also, it seems to me, equally plain that a State system of involuntary insolvency also remains in full operation upon persons and corporations, who are as possible bankrupts within the operation of the National Bankruptcy Act, so far as the State system deals with cases of which the bankrupt courts under the Federal act can obtain no jurisdiction. To state the point otherwise, I may say that to my mind there is no distinction between an insolvent insurance company, railroad company or laundry company, which owes \$1,000 of debts and has committed an act of bankruptcy, on the one hand, and an insolvent manufacturing, mercantile or trading company which has committed no act of bankruptcy, or does not owe debts amounting to \$1,000, on the other hand, in respect of the operation of the National Bankrupt Act and the New Jersey Insolvent Corporation Act. In neither instance is a case presented of which the Federal bankrupt court can take cognizance. Each case, therefore, is within the full and complete operation of the New Jersey statute."

In re F. A. Hall Co., 10 A. B. R. 96, 121 Fed. 992 (D. C. Conn.): "* * * by its terms, it went into full force and effect upon its passage, and, ipso facto, at

once suspended and superseded all State insolvent laws. Whether it cuts any deeper it is unnecessary to inquire at the present juncture. It is not important that by an express provision of the Bankruptcy Act a corporation is excepted from the category of those who are permitted to enjoy its privileges as voluntary bankrupts. A way is provided by which the district courts can and do acquire and retain jurisdiction of the property which, before the passage of the act, could and would have been administered by the probate court."

Parmenter Mfg. Co. v. Hamilton, 1 A. B. R. 40, 172 Mass. 178: "The act is 'to go into full force and effect upon its passage.' That is to say, the rights of all persons in the particulars to which the act refers are to be determined by the act from the time of its passage. Among these rights is the right to have insolvent estates settled in bankruptcy under the provisions of the act, including the rights to have acts of bankruptcy affecting the settlement of estates determined by it (§ 3), to have the rights of debtors to file voluntary petitions and of creditors to file involuntary petitions determined by it (§ 4), and to have preferences and liens governed by the provisions of it (§§ 60 and 67).

"These various provisions affecting the rights and conduct of debtors and creditors are different from those previously existing in most of the States, and perhaps different from those found in the laws of any State; and they supersede all conflicting provisions."

In *re Bruss-Ritter Co.*, 1 A. B. R. 58, 90 Fed. 651 (D. C. Wis.): "The power of Congress to enact a general bankruptcy statute is secured by constitutional provision. In the absence of such congressional enactment the States are free to provide for insolvency relief of limited extent; but when Congress exercises its authority by a general enactment all State action is suspended from such time, and subject only to such limitations as may be prescribed in the act. *Tua v. Carriere*, 117 U. S. 201, 209-10. As remarked in *Platt v. Archer*, 9 Blatch. 559; Fed. Cas. No. 11,213, this authority of Congress 'is paramount and exclusive, and so is the jurisdiction of the District Court thereunder.' The doctrine thus stated is well established, and is unquestioned upon this motion."

In *re McKee*, 1 A. B. R. 311 (Ky. County Court): "To whatever extent Congress has undertaken to provide remedies and prescribe procedure, its authority, being unquestionably paramount, State statutes designed for the same or similar purposes must give way. It cannot be, for a moment, presumed that Congress, having full power to prescribe the sole method of procedure, intended to allow concurrent jurisdiction to State courts, which might, acting under different statutes and governed by different precedents, reach entirely different conclusions than those entertained by the Federal courts, nor can it be reasonably contended, that it was ever contemplated, that the same, or similar, remedies, should be exercised by both State and Federal courts, thereby unnecessarily subjecting all parties to double labor and annoyance, and vastly increasing the costs of administering these trusts. Any other construction of this act must ignore the cardinal principle of uniformity, in the settlement and distribution of insolvent estates, that was made the basis for the constitutional provision, under which all national acts of bankruptcy have been passed."

§ 1629. State Insolvency and Bankruptcy Laws Ipso Facto Suspended.—State insolvency and bankruptcy laws are ipso facto suspended (as to the same classes covered by the Federal Bankruptcy Act) no matter whether federal bankruptcy proceedings follow in the particular case involved or not: the state court will not have jurisdiction.²⁷

²⁷. *Ketcham v. McNamara*, 6 A. B. R. 160, 72 Conn. 709; *Littlefield v. Gray*, 8 A. B. R. 409, 52 Atl. 925 (Me.); *obiter*, In *re Sievers*, 1 A. B. R. 117, 91

Potts v. Smith Mfg. Co., 12 A. B. R. 392, 25 Pa. Superior Ct. 206: "The only cases decided by courts of last resort holding a different view, which have come under our observation, are *In re Ziegenfuss*, 2 Ired. 463, and *Reed v. Taylor*, 32 Ia. 209. These cases recognize the paramount authority of the Act of Congress, but hold that the State statute is operative up to the time when proceedings are instituted under the National Bankrupt Act. The efficiency of the State statute is made to depend upon action or nonaction under the Bankrupt law. This seems a foundation entirely too unsubstantial upon which to base the right to proceed under the State law, as to persons and subjects affected by the National Bankrupt Act. The law would be vain which would invite legal process liable to be avoided and defeated at any stage of the proceedings by the assertion of another and paramount authority; it should be effective for the purpose of carrying to conclusion proceedings instituted thereunder. It is conceded on all sides, however, that any proceedings under the insolvent law of the State might be rendered abortive by an insolvent debtor or his qualified creditors by filing a petition in bankruptcy where the debtor was subject to the operation of the National Bankrupt Act. The national and State laws are intended, in a large degree, to operate upon the same persons and property, and while there is a close resemblance in the methods of administration, the mode of procedure and remedies are not the same. There might, and doubtless would be, conflict in the operation of the national and State statutes. The latter must, therefore, yield to the former. The uniformity contemplated by the Constitution can only be secured through the Act of Congress, the prosecution of insolvent proceedings under the laws of the various States necessarily tending to confusion and lack of uniformity.

"In view of the manifest purpose of the constitutional provision on the subject of bankruptcy and the great weight of authority in support of the conclusion reached we feel constrained to hold that the Act of June 4, 1901, relating to insolvency, did not become operative, because of the existence of the bankruptcy law of the United States of July 1, 1898, as to the persons and subjects to which the latter act applies. The order of the court of June 23, 1903, vacating and setting aside the execution of the plaintiff is, therefore, reversed."

Apparently, although obiter, *In re Richard*, 2 A. B. R. 506, 94 Fed. 633 (D. C. N. Car.): "* * * the State law is suspended and inoperative after an adjudication in bankruptcy. The Bankrupt Court takes jurisdiction of the estate and all matters pertaining thereto, and will administer the same to a final settlement."

Apparently, *In re Allison Lumber Co.*, 14 A. B. R. 79, 137 Fed. 643 (D. C. Ga.): "The enactment by Congress of a uniform system of bankruptcy has

Fed. 366 (D. C. Ky.); *In re Hall*, 10 A. B. R. 88 (D. C. Conn.); *Moody v. Port Clyde Development Co.*, 18 A. B. R. 275 (Sup. Ct. Me.); compare, obiter, in *Carling v. Seymour Lumber Co.*, 8 A. B. R. 29, 113 Fed. 483, C. C. A. Ga., reversing, on other grounds, *In re Macon Sash, Door & Lbr. Co.*, 7 A. B. R. 66; apparently, *In re Smith & Dodson*, 2 A. B. R. 9 (D. C. Ind.); *In re Macon Sash, Door & Lumber Co.*, 7 A. B. R. 66 (D. C. Ga., reversed on other grounds—comity—in *Carling v. Seymour Lbr. Co.*, 8 A. B. R. 29, 113 Fed. 483, C. C. A. Ga.); inferentially,

Parmenter Mfg. Co. v. Hamilton, 1 A. B. R. 41 (Supreme Ct. Mass.); inferentially, *In re Bruss-Ritter Co.*, 1 A. B. R. 58, 90 Fed. 651 (D. C. Wis.); *In re Curtis*, 1 A. B. R. 440, 91 Fed. 737 (D. C. Ills.); obiter, *Patty-Joiner Co. v. Cummins*, 4 A. B. R. 269, 67 S. W. 566 (Tex. Sup. Ct.); impliedly, *Wescott v. Berry*, 4 A. B. R. 264, 45 Atl. 352 (N. H. Sup. Ct.); *Griswold v. Pratt*, 50 Mass. 16, as to Act of 1841; *In re Pickens Mfg. Co.*, 20 A. B. R. 202, 166 Fed. 585 (D. C. Ga.); *In re Weedman Stave Co.*, 29 A. B. R. 460, 199 Fed. 948 (D. C. Ark.).

been repeatedly held to suspend the operation of State bankruptcy or State Insolvency Laws."

Some cases seem to hold that they are void only on the subsequent institution of federal bankruptcy proceedings; but on analysis such cases will be found not to be cases under state bankruptcy nor state insolvency laws but rather to be cases under division 1 or 2 of this chapter relating to the custody of property where there are legal liens nullified by bankruptcy, or where an assignment or receivership has been created, voidable only in case of bankruptcy within four months.

§ 1630. Not Suspended nor Inoperative as to Classes Not Covered by Federal Bankruptcy Act.—State insolvency and bankruptcy laws are not suspended nor rendered inoperative, nor void at all, as to those classes of persons exempted from, or not included within, the operation of the federal act.²⁸

Old Town Bank *v.* McCormick, 96 Md. 341, 10 A. B. R. 767: "This brings us to the real question in the case, namely, Is there any conflict between our Insolvent Law and the Federal Bankrupt Law? We have already transcribed the provisions of § 4, by which it appears that the defendant is expressly excepted from the provision of the act relating to involuntary bankruptcy, and therefore as to this class to which the defendant belongs (i. e., farmers or tillers of the soil) the Federal power has not been exercised. And it therefore follows that, if this class is not within the State law, there is no existing provision under which those embraced within it can be compelled to distribute their assets fairly and equally among their creditors. In Geery's Appeal, 43 Conn. 289, 21 Am. Rep. 653, it was said: 'The benefit of this principle [the equal distribution of a debtor's property without preference] cannot be denied to a creditor without doing him injustice. It is a remedy which he relied on in giving credit, and to which he is fairly entitled. If that remedy is not to be found in the Bankrupt Act, it will not be presumed that Congress intended to take away the remedy provided by the State. Congress having limited and restricted the operation of the Bankrupt Act, leaving a number of cases to which it does not apply, it will not be presumed that it was thereby intended to leave creditors in such cases entirely without remedy, as must be the case if the State law is entirely inoperative. But can it be properly or correctly said that any conflict can exist between the State and Federal law so long as the latter by express terms excludes from its operation the subject or class of persons expressly provided for by the State law? The power to enact insolvent or bankrupt laws is vested in the States, and it cannot be extinguished except by the establishment of a Federal system in conflict with the State law. And this Federal system of bankruptcy must be a genuine bankrupt law (*Sturgis v. Crownshield*, 4 Wheat. 122, 4 L. Ed. 529), or, in other words, as expressed in *Ogden v. Saunders*, 12 Wheat. 213, 6 L. Ed. 606, the power to pass a uniform system of bankruptcy must be actually exercised, and the State law must be in conflict with it in order to render the latter inoperative. The question, therefore, logically arises. Does the present Federal Bankrupt Law actually provide for involuntary proceedings against farmers? And

²⁸. *Singer v. Nat'l Bedstead Mfg Co.*, 11 A. B. R. 276 (N. J. Ch.), quoted ante, at § 1628. (1841) Also, see *Ex*

parte *Eames*, 2 Story 322, 323, Fed. Cas. 4,237.

the answer must be that it does not, but the answer of the defendant goes further and necessarily must do so in order to save his case. He says it is true that while this class is not included in, and is expressly excepted from, the involuntary feature of the system, yet it is included in the voluntary feature, and therefore it is within the scope of the national system. We cannot approve of this method of reasoning, not only because it would seem to be a 'contradiction in terms to say that cases excepted from the operation of the most important part of the act are included in its scope,' but because it would seem to involve the proposition that the Federal power can render inoperative the State insolvent laws applicable to involuntary insolvency, without establishing a genuine bankrupt law to take the place of the State law. As we have already seen, it has been held from an early day that it is only to the extent that Congress has actually legislated upon the subject that the statutes of the several States are suspended by its legislation. How, then, can it be said that a failure to legislate—in other words, an express exclusion—raises a conflict? But without pursuing this question further, it seems to us that the position taken by the defendant must necessarily lead to the conclusion that if the Congress of the United States can, by including this class in the voluntary part of the system, and excepting it from the involuntary part, withdraw it from the operation of our State Insolvent Law, it can do the same in regard to any two or more classes (as, for instance, merchants, traders, and corporations); and the result would be that, in spite of the failure on the part of Congress to establish a bankrupt law (that is, to actually exercise the power conferred by the Constitution to pass a genuine bankrupt law, State legislation would become inoperative, and creditors would be deprived of a remedy to which, as was said in *Gerry's Appeal*, 43 Conn. 289, 21 Am. Rep. 653, they are fairly entitled.

"But it was forcibly argued on the part of the defendants that § 70, subsection 'b,' of the Bankrupt Act of 1898, shows that it was the intention of Congress to substitute that act for every provision of every insolvent law of the several States. It provides as follows: 'Proceedings commenced under State insolvent laws before the passage of this act shall not be affected by it.' To sustain their view, the case of *Parmenter Mfg. Co. v. Hamilton*, 1 A. B. R. 39, 172 Mass. 178, decided in 1898 was relied on. But all this case decides is that the Federal act deprives the State court of jurisdiction to entertain jurisdiction in insolvency proceedings filed after 1st July, 1898, when the Federal act went into force. Or as the court said: 'The act is to go into full force and effect upon its passage. That is to say, the rights of all persons, in the particulars to which the act refers, are to be determined by the act from the time of its passage.' After mentioning a number of the rights which are determined by the act, the opinion continues: 'These various provisions affecting the rights and conduct of debtors and creditors are different from those previously existing in most of the States, and perhaps different from those found in the laws of any State, and they supersede all conflicting provisions.' In the concluding part of the opinion the distinguished judge who has recently been appointed chief justice of the Supreme Judicial Court of Massachusetts said that the language of § 70, subsection 'b,' 'was chosen to make clear the purpose of Congress that the new system of bankruptcy should supersede all State laws in regard to insolvency from the date of the passage of the act;' but necessarily this language means only that all conflicting provisions of the State law were thus superseded, for this is the well-settled proposition which he had just announced in a preceding sentence, and which we have quoted above. If, therefore, we are correct in the conclusion already reached, that there is no conflict between the provisions of our Insolvent Law and the present Bankrupt Law, it follows that the language of § 70 relied on by the defendant can have no influence upon our conclusion in this case."

"But again, it was urged that there is a distinction between this case and cases which arose under laws which did not include the class within its scope—as, for instance, where the Bankrupt Act applied only to debtors whose debts exceeded \$300. It was held in *Shephardson's Appeal*, 36 Conn. 23, that in cases where the debts were less than \$300 the State law was not suspended, and debtors of that class could be proceeded against under State laws. But the true rule was laid down by Chief Justice Marshall in *Sturgis v. Crowninshield*, 4 Wheat. 122, 4 L. Ed. 529, that the power of the State continues to exist over such cases as the Federal law does not reach. And, therefore, if cases involving involuntary proceedings against a class are not provided for by the Federal law, such cases are within the reach of the State law, in spite of the fact that the members of this same class may avail themselves of the voluntary feature; otherwise the rule laid down by Chief Justice Marshall would have to be changed so as to read that the power of the State exists only over such cases as are against natural persons or corporations not within any class provided for by any provision of the Federal law. If this were the rule, then, of course, it would follow, as contended, that the defendant, being of the class called 'Farmers,' and the Bankrupt Act having provided that he may avail himself of the voluntary feature, no case against him could be reached by the State law. But, in our opinion, this is not the proper view, for, as we have already said, it is not within the power of Congress to render inoperative the involuntary feature of State insolvent laws as to any particular class by excepting that class from the involuntary part of the national law. Otherwise the result would be that the State laws as to involuntary insolvency would become inoperative by the mere existence of the power of the United States to establish a system of involuntary bankruptcy. We have seen, however, that it is not the mere existence, but the exercise of the power to establish a genuine bankrupt law in conflict with the State laws, which renders the latter inoperative."

Herron Co. v. Superior Court, 8 A. B. R. 492, 68 Pac. 814, 136 Calif. 279: "If the Bankruptcy Act excepts a class of cases from its operation, either in express terms or by necessary implication, it must be considered that it was the intention of Congress not to interfere in that class of cases with the laws of the several States in reference thereto. The State laws will remain operative in all cases which are not within the provisions of the Bankruptcy Act. * * * Congress may enact a bankruptcy act for certain classes of creditors, and leave to the several States the right to legislate upon the subject with reference to other classes. In such a case there can be no conflict of jurisdiction, as the legislation of the two governments is not upon the same subject. Each statute is operative within its own jurisdiction, and may be enforced without in any respect infringing upon the jurisdiction of the other.

"The Bankruptcy Act passed by Congress in 1898, is not operative upon all classes of creditors, or upon all classes of corporations."

Thus, in the case, *The Old Town Bank v. McCormick*, 96 Md. 341, the court held that a State insolvency law by which persons engaged chiefly in the tillage of the soil may be proceeded against in involuntary insolvency by their creditors, is not superseded as to such persons by the Federal Bankruptcy Act of 1898.

Again, unless a corporation is among the classes that can be proceeded against in bankruptcy it is still subject to the State insolvency law.²⁹

29. *Herron Co. v. Superior Court*, 8 A. B. R. 492, 68 Pac. 814, 136 Calif. 279: A mining corporation before the

Amendments of 1903 and of 1910 included such corporations.

Nor are state insolvency or bankruptcy laws suspended as to those persons who have done acts not mentioned as acts of bankruptcy in the federal law but which are prohibited by or come within the purview of the state insolvency law:³⁰

McCullough v. Goodhart, 3 A. B. R. 85 (Penn. Com. Pleas): “* * * the bankruptcy law of 1898 does not contain any enactment concerning absconding or concealed debtors, and therefore does not come in conflict in any way with the State law relating to domestic attachment.”

Nor as to acts committed before the passage of the Federal Bankruptcy Act.³¹

Other decisions hold broadly that the state insolvency proceedings are absolutely null and void and inoperative as to any person who, either involuntarily or voluntarily, could become subject to the operation of the federal bankruptcy law.

Littlefield v. Gray, 8 A. B. R. 409, 52 Atl. 925 (Me.): “The question here involved is whether the insolvency law of this State is superseded by the Bankruptcy Act of the United States as to debtors owing more than \$300 and less than \$1000.

“The insolvency law of this State is not wholly superseded by the Bankrupt Act, but when they come in conflict the latter must prevail. *Damon's Appeal*, 70 Me. 155. So far as the person and subject-matter fall within the provisions of the Bankrupt Act, and are within the jurisdiction of the bankrupt court, the State Insolvency Law is superseded and cannot be revoked. *Bank v. Ware*, 95 Me. 395, 50 Atl. 24; *Ogden v. Saunders*, 12 Wheat. 213, 6 L. Ed. 606; *Ex parte Eames*, 2 Story, 324, Fed. Cas. No. 4,237.

“In the case before us, *Blackington*, the insolvent debtor, owing less than \$1,000, was petitioned into insolvency in 1899 by his creditors, while the United States Bankrupt Act was in force. The State insolvency court took jurisdiction, decreed him insolvent, and appointed the plaintiff assignee. This action is to set aside a conveyance by *Blackington*, as a preference under the State law.”

“Under the Bankrupt Law, *Blackington* could have gone into bankruptcy voluntarily, but could not be forced in by his creditors under involuntary proceedings. He was asked to go in and refused. It was argued with great ability that in that condition the State insolvency law may be invoked. Plausible as the argument is, we do not regard it as sound. At any time after proceedings under the State Law, *Blackington* could have voluntarily invoked the Bankrupt law, and thereupon all proceedings under the State law would necessarily cease. The test of jurisdiction under the State law does not rest upon the volition of the debtor. If his person and property are or may be subject to the Bankrupt Law, then as to him and his possession the State insolvency law is in abeyance and powerless. Upon any other view, it would be in the power of the debtor at any time to oust the jurisdiction of the State court after it had been assumed. This would result in great confusion. It may be avoided by holding, as we do, that where the person falls within the purview of the Bankrupt Act, whether by voluntary or involuntary proceedings, the State insolvency law must be silent.

30. *Singer v. Nat'l Bedstead Mfg. Co.*, 11 A. B. R. 276 (N. J. Ch.), which was a case of dissolution of a corporation.

31. *Grunsfeld Bros. v. Brownell*, 11 A. B. R. 603 (Sup. Ct. New Mex.).

"When this case was previously before the court (52 Atl. 925), we said that there might be cases where the insolvency court would have jurisdiction, notwithstanding the Bankruptcy Act. If such cases can arise, it can only be in instances not within the purview of the Bankrupt Act, where its provisions cannot be invoked either by the debtor or his creditors. This case does not fall within that rule.

"It follows that the insolvency court was without jurisdiction in this case, and an appointment of plaintiff as assignee was unauthorized and void. He therefore has no standing in court."

In re F. A. Hall Co., 10 A. B. R. 96, 121 Fed. 992 (D. C. Conn.): "It is not important that by an express provision of the Bankruptcy Act a corporation is excepted from the category of those who are permitted to enjoy its privileges as voluntary bankruptcy. A way is provided by which the district courts can and do acquire and retain jurisdiction of the property which, before the passage of the act, could and would have been administered by the probate courts."

There is considerable force in the argument of the court in *Littlefield v. Gray*, and in *In re Hall*, *supra*, that when the framers of the Constitution gave over to Congress the function of making uniform laws "on the subject" of "bankruptcies" throughout the United States, it must have been their intention that the laws passed by Congress in relation to "bankruptcies," whether including or excluding certain classes of persons, should be the only laws relating to bankruptcies that should be considered to be in force; and that it would follow that persons whom Congress upon grounds of public policy deemed best to exempt from bankruptcy, thereby have been given protection against all kinds of bankruptcy proceedings; also, that Congress having been given exclusive jurisdiction over the entire "subject" of "bankruptcies," and having spoken as to what classes may be proceeded against and as to what may not be proceeded against, those exempted and those included are equally within the scope of its mandate; and that therefore when the States attempt to enforce bankrupt laws of their own, they are encroaching on the functions given by the federal Constitution to Congress, there being no more power in them to nullify the exemptions or exceptions granted by Congress than to nullify the prohibitions.

While the main proposition (*ante*, § 1628), undoubtedly states the true rule as far as it goes, it is not to be assumed that all state bankruptcy or state insolvency proceedings not within the terms of the rule are necessarily not superseded. The converse of the main proposition is not necessarily true. The converse may be stated as follows: It being true that whenever Congress passes a national bankrupt act that act is paramount as far as it speaks, by virtue of the Constitution, and supersedes ipso facto all state insolvency and bankruptcy laws in case the National Bankrupt Act itself so provides; yet, in case it does not so provide, it supersedes the state insolvency and bankruptcy laws *only to the extent that it makes the particular persons mentioned therein subject thereto upon the doing of the particular acts mentioned therein as grounds for its involuntary action*; it being necessary that the person and the act both be within its purview,

else it will not supersede the state law in the particular case. This converse rule is laid down in *Singer v. Nat'l Bedstead Co.*, supra.

But this converse rule will have to be still further limited by the qualification that the state and federal proceedings must both be involuntary or both voluntary; otherwise no natural person could be proceeded against in state bankruptcy proceedings since all natural persons may go voluntarily into bankruptcy. Interesting questions arise under this construction. Thus, what would be the situation, for instance, as to a natural person who owes less than \$500 of debts and whom creditors are seeking to proceed against in state bankruptcy proceedings: is he or is he not exempt from all bankruptcy proceedings against him, state as well as federal, by virtue of his express exemption under the Federal Act? Or, suppose he has perpetrated an act forbidden by state bankruptcy law and not by the federal bankruptcy law: does he remain liable to proceedings under the state law and will the state bankruptcy court retain jurisdiction of his assets if he goes voluntarily into bankruptcy under the federal law within four months?

The reasoning of *Singer v. Nat'l Bedstead Co.* in its statement of the converse rule is exceedingly broad, and the difficulties in the way of adopting its construction are quite serious.

§ 1631. State Bankruptcy and Insolvency Laws Simply Held in Abeyance.—The state insolvency and state bankruptcy laws are simply held in abeyance whilst the federal bankruptcy statute is in operation, and upon the repeal of the federal bankruptcy statute, the state insolvency and bankruptcy laws spring again into full vigor without re-enactment.³²

In re Wright, 2 A. B. R. 592, 95 Fed. 807 (D. C. Mass., affirmed sub nom. In re Worcester Co., 4 A. B. R. 506): "An insolvent law may be amended, repealed, or enacted by a State during the existence of the Bankrupt Law; and such amendment, repeal, and enactment will be valid legislative acts, though the operation of these acts in some respects be suspended while the Bankrupt Law continues in force. When the Bankrupt Law has been repealed, the insolvent laws of the States become operative; and, if amended during the existence of the Bankrupt Law, they doubtless become operative in their amended form. Counsel for the trustee sought in argument an analogy between the insolvent

³². *Sturgis v. Crowninshield*, 4 Wheat. 122, quoted ante, § 1627; obiter, *Littlefield v. Gray*, 8 A. B. R. 409 (Sup. J. Ct. Mo.). See editor's note, *Parmenter Mfg. Co. v. Hamilton*, 1 A. B. R. 41 (Sup. Ct. Mass.); In re Worcester County, 4 A. B. R. 506, 102 Fed. 808 (C. C. A. Mass.); *Butler v. Goreley*, 146 U. S. 314.

State insolvency proceedings begun before the passage of the Bankruptcy Act are not affected thereby, *Bankr. Act*, § 70 (b); *Wescott Co. v. Berry*, 4 A. B. R. 264, 45 Atl. 352 (N. H. Sup. Ct.); also, *Osborn v. Fender*, 11 A. B. R. 224, 92 N. W. 1114 (Sup. Ct. Minn.);

compare, to same effect, *Ex parte Eames*, 2 Story 322, 325.

And an assignee or receiver appointed in an insolvency proceeding so begun before the passage of the Bankrupt Act may commence or maintain a suit to recover property fraudulently conveyed or concealed, *Osborn v. Fender*, 11 A. B. R. 224 (Sup. Ct. Minn.).

And State insolvency and bankruptcy laws may be looked to and their priorities be adopted under § 64 (b) (5) though their operation otherwise be suspended, see post, "Priorities Given by Federal and State Laws," §§ 2196 and 2197.

laws thus suspended and law unconstitutional, and therefore void, but the analogy is very imperfect. To establish that the insolvent laws of the several States now upon their statute books are not 'laws of the States,' it must be shown that they are not laws at all; that they are wholly void, and not merely restricted in their application. Inasmuch, therefore, as the Bankrupt Act of 1898 expressly recognizes the existing validity of these insolvent laws as applied to proceedings commenced before the passage of the Bankrupt Act, and inasmuch as the insolvent laws revive, *ex proprio vigore*, on the repeal of the Bankrupt Law, it follows that the insolvent laws have not been wholly void but are still laws of the States which adopted them."

Of course mere general assignments are an entirely different thing, as we have heretofore seen; and they are not involved in the discussion as to whether or not insolvency laws are suspended by the bankruptcy act.³³

§ 1632. Bankruptcy and Insolvency Laws, and General Assignment Laws, Distinguished.—There have been many finely drawn distinctions made between insolvent laws and bankruptcy laws but the courts do not seem to have struck an exact line of demarkation.³⁴

Hanover Nat'l Bank v. Moyses, 186 U. S. 181, 8 A. B. R. 1: "The whole subject is reviewed by that learned commentator in chapter 16, §§ 1102 to 1115, of his work, and he says (§ 1111) in respect of 'what laws are to be deemed bankrupt laws within the meaning of the Constitution:' 'Attempts have been made to distinguish between bankrupt laws and insolvent laws. For example, it has been said that laws which merely liberate the person of the debtor are insolvent laws, and those which discharge the contract are bankrupt laws. But it would be very difficult to sustain this distinction by any uniformity of laws at home or abroad. * * * Again, it has been said that insolvent laws act on imprisoned debtors only at their own instance, and bankrupt laws only at the instance of creditors. But, however true this may have been in past times, as the actual course of English legislation, it is not true, and never was true, as a distinction in colonial legislation. In England it was an accident in the system, and not a material ground to discriminate, who were to be deemed in a legal sense insolvents, or bankrupts. And if an act of Congress should be passed, which should authorize a commission of bankruptcy to issue at the instance of the debtor, no court would on this account be warranted in saying that the act was unconstitutional, and the commission a nullity. It is believed that no laws ever were passed in America by the colonies or States, which had the technical denomination of "Bankrupt laws." But insolvent laws, quite co-extensive with the English bankrupt system in their operations and objects, have not been unfrequent in colonial and State legislation. No distinction was ever practically, or even theoretically, attempted to be made between bankruptcies and insolvencies. And a historical review of the colonial and State legislation will abundantly show that a bankrupt law may contain those regulations which are generally found in insolvent laws, and that an insolvent law may contain those which are common to bankrupt laws.'"

Sturges v. Crowninshield, 4 Wheat 122, 195: "The Bankrupt Law is said to grow out of the exigencies of commerce, and to be applicable solely to traders:

33. But see *In re Scholtz*, 5 A. B. R. 782, 106 Fed. 834 (D. C. Iowa), where the court fails to make the distinction, although deciding rightly that the Iowa general assignment law is

not suspended by the Bankruptcy Act but is only superseded as to the particular bankruptcies involved.

34. *Grunsfeld Bros. v. Brownell*, 11 A. B. R. 602 (N. Mex. Sup. Ct.).

but it is not easy to say who must be excluded from, or may be included within this description. It is like every other part of the subject, one on which the legislature may exercise an extensive discretion. This difficulty of discriminating with any accuracy between insolvent and bankrupt laws, would lead to the opinion that a bankrupt law may contain those regulations which are generally found in insolvent laws; and that an insolvent law may contain those which are common to a bankrupt law."

Also much has been said as to whether a particular law has amounted to an insolvency or bankruptcy law, or is a mere assignment law. There is a substantial difference between a proceeding under a state insolvency statute, and one under a state statute permitting general assignments.³⁵

Ketcham v. McNamara, 6 A. B. R. 161, 72 Conn. 709: "These statutes constitute, in the fullest sense, an insolvent law. They make the title under a general assignment executed by an insolvent debtor in trust for the benefit of all his creditors, which is lodged for record in the Court of Probate, only an inchoate one. To perfect it, requires a judgment of confirmation from that court. Nor, when perfected, is the estate assigned to be applied as directed by the terms of the conveyance. Creditors do not share equally. Certain claims for the wages of labor may be preferred."

These discussions are pertinent because it seemed, at least formerly, to have been conceded to be the rule that the passage of a federal bankruptcy statute ipso facto suspends all state insolvency and bankruptcy laws, no matter whether bankruptcy proceedings under federal law were brought within four months, or, for that matter, were ever brought, although it was conceded that mere general assignments for the benefit of creditors were invalidated only in case bankruptcy followed and followed within the four months period.³⁶

Thus, it was held by the United States Supreme Court during the existence of the old bankruptcy law of 1867, in the case of *Mayer v. Hellman*, 91 U. S. 496, that the Ohio system of administering voluntary assignments for the benefit of creditors did not amount to an insolvency law, and that a general assignment, therefore, was not absolutely void from the very beginning, but was merely voidable by the institution, within the prescribed time, of federal bankruptcy proceedings. In that case, the bankruptcy occurred more than six months after the assignment, so it had become pertinent to ascertain whether the assignment proceedings were absolutely void or only voidable.³⁷

35. In *re Sievers*, 1 A. B. R. 117, 91 Fed. 366 (D. C. Mo., affirmed in 1 A. B. R. 412). But see *In re McKee*, 1 A. B. R. 311 (Ky. Co. Ct.), where assignment cases are included within the same rules.

36. In *re Sievers*, 1 A. B. R. 117, 91 Fed. 366 (D. C. Ky., affirmed in 1 A. B. R. 412). Compare, *In re Smith & Dodson*, 2 A. B. R. 9, 92 Fed. 135 (D. C. Ind.).

37. *Mayer v. Hellman*, 91 U. S. 496

(cited in *In re Plotke*, 5 A. B. R. 171, C. C. A. Ills., and followed in *Simonson v. Sinsheimer*, 3 A. B. R. 824, 95 Fed. 952; and distinguished as based on assignment made before four months period in *In re Chase*, 10 A. B. R. 684, 124 Fed. 753, C. C. A. R. I.).

Patty-Joiner Co. v. Cummins, 4 A. B. R. 269, 57 S. W. 566 (Tex. Sup. Ct.), which was a case of a general assignment under a State Law permitting the debtor to exact a release from any

If we are to be guided at all by the history of bankruptcy legislation during the last four hundred years, it is obvious that in order for any system to amount to a bankruptcy system, it must provide machinery for the throwing of a debtor into insolvency involuntarily, and for completely administering his assets; and that, if a system of laws does so operate, then it is a bankruptcy system no matter by what name it might be designated. General assignment laws do not have this operation. Primarily, such laws simply provide a system for the administration of voluntary assignments in trust. That is to say, it has always, of course, been possible for a debtor to deed his property in trust to pay all, or some class of his creditors, and chancery always has had jurisdiction to compel such trusts to be properly carried out, precisely as it has as to any other trusts. Indeed, in the *Mayer v. Hellman* case it appears that originally such trusts for the benefit of creditors were simply administered in the Common Pleas Court of the State like any other trust, and no special court, like the probate or insolvency court, had jurisdiction. The Supreme Court in that case seems to have held that simply because such trusts subsequently were taken out of the Common Pleas Court and given over to a special court for administration, did not effect a change in their essential features; and that they were not absolutely void, but merely voidable.³⁸

Compare to this effect, *In re Gutwillig*, 1 A. B. R. 81, 90 Fed. 475 (D. C. N. Y., approved in *Lea v. West*, 174 U. S. 590): "Proceedings like those under the Massachusetts act rest wholly upon State statutes. Such statutes are practically bankruptcy acts, operating, however, only to the extent of the power and jurisdiction of State authority.

"Voluntary assignments for the benefit of creditors, on the other hand, as practised in this and other States, do not originate in the State statutes, but in the common-law power of the debtor to dispose of his property. The statutes of this State passed in 1860, and subsequent acts, regulate to a certain extent this power of distribution, and provide various securities therefor. To a considerable extent, therefore, these statutes, and assignments made in conformity with them, though they make no provision for the discharge of the debtor, do cover in part the original purpose of bankruptcy laws, namely, the equal distribution of the debtor's property among his creditors. The New York Statutes, nevertheless, allow, besides preferences to employees, preferences to other creditors, at the debtor's option, to the extent of one-third of the assets (see *Central N. Bank v. Seligman*, 138 N. Y. 435); in this regard being, therefore, directly opposed to that equality of distribution which bankruptcy laws aim to secure. Though the precise limits of the terms 'bankruptcy' and 'insolvency,' in defining the character of statutes, may not be easy to determine (see *Sturges v. Crowninshield*, 4 Wheat 194-6; *In re Klien*, 1 How. (U. S.) 277, I do not think that a general assignment made in conformity with laws like those of the

creditor as a condition of receiving any benefit.

In *re Romanow*, 1 A. B. R. 461, 92 Fed. 510 (D. C. Mass.); [1867] *Boese v. King*, 108 U. S. 379. Compare, *In re Farrell*, 23 A. B. R. 826, 176 Fed. 505 (C. C. A. Ohio), quoted post.

³⁸. Compare, to this effect, *Duryea v. Guthrie*, 11 A. B. R. 234 (Sup. Ct. Wis.); *Patty-Joiner Co. v. Cummins*, 4 A. B. R. 269, 57 S. W. 566 (Tex. Sup. Ct.); *In re Curtis*, 1 A. B. R. 440, 91 Fed. 737 (D. C. Ills.).

State of New York, can be considered 'as a proceeding commenced under State insolvency laws' within the meaning of the last paragraph of the Act of 1898; and the question presented on this motion must therefore be decided upon the general principles of bankruptcy law and upon the other provisions found in the present act."

Likewise in Missouri, see *In re Sievers*, 1 A. B. R. 117, 91 Fed. 366 (D. C. Mo.): "While the insolvency laws of the several States are superseded by the enactment of the National Bankrupt Law, this is not the case with State statutes which merely regulate the administration of the trust created by an assignment for the benefit of creditors; and proceedings under such statutes or under a common law deed of assignment are not void or voidable by reason of the existence merely of a Bankrupt Law or unless proceedings in bankruptcy are subsequently instituted against the assignor."

Compare, *Grunsfeld Bros. v. Brownell*, 11 A. B. R. 603, 12 N. Mex. 192: "No one can contend that the passage of a bankruptcy act by Congress would render void a general common-law deed of assignment made by a debtor conveying all of his property for the benefit of his creditors ratably according to their claims, but not providing for the release of the debtor. It would be perfectly valid as to all men unless they seasonably took proceedings under the Bankruptcy Act."

As to whether a proceedings is an insolvency proceedings or not, the test is what can be accomplished under it—will it operate to supplant the federal act.³⁹

It is probably not essential to the idea of a bankruptcy or insolvency law that it shall provide for the discharge of the debtor.⁴⁰

In re Salmon & Salmon, 16 A. B. R. 134, 143 Fed. 395 (D. C. Mo.): "Again, to render a state insolvency law inoperative because in contravention of the federal bankrupt act, it is not essential that the State Act shall contain a provision for the discharge of the debtor. It is rather thought such provision for discharge is an incident to, but not an essential part of such law."

The holding of the state courts as to whether an assignment law amounts to a general insolvency statute will control.⁴¹

It is to be remarked that the courts have re-enunciated the doctrine of *Mayer v. Hellman*, as to the Ohio statute regulating assignments for the benefit of creditors.

In re Farrell, 23 A. B. R. 826, 176 Fed. 505 (C. C. A. Ohio): "This, [Ohio Revised Statutes, § 6335] as pointed out in *Mayer v. Hellman*, presupposes the existence of a deed of assignment and creation of a trust, and simply undertakes to regulate the trust later for the equal protection of the creditors. The right so to dispose of the property in trust is not dependent upon the statute; it is an ordinary attribute of ownership. * * * Section 6343 of the Revised Statutes of Ohio was amended twice (in 1898 and in 1902) between

39. *In re Macon Lumber Co.*, 7 A. B. R. 66, 112 Fed. 322 (D. C. Ga., reversed, on other grounds, sub nom. *Carling v. Seymour Lumber Co.*, 8 A. B. R. 29, 113 Fed. 483, C. C. A. Ga.). Compare, *In re McKee*, 1 A. B. R. 311 (Ky. Co. Court).

40. Compare, to similar effect, *In re*

Hall Co., 10 A. B. R. 88, 121 Fed. 992 (D. C. Conn.); *In re Curtis*, 1 A. B. R. 440, 91 Fed. 737 (D. C. Ills.); *In re Marshall Paper Co.*, 4 A. B. R. 468, 102 Fed. 872 (C. C. A. Mass.); (1867) *In re Reynolds*, Fed. Cas. No. 11,723.

41. *In re Curtis*, 1 A. B. R. 440, 91 Fed. 737 (D. C. Ills.).

the times when the decisions just mentioned [*Mayer v. Hellman*, 91 U. S. 496, and *Boese v. King*, 108 U. S. 379] were rendered, and the dates of the general assignment and the filing of the petition in bankruptcy in question. * * *. It cannot escape attention, moreover, that both of these changes plainly tended to remove, rather than to enhance, conflict between § 6343 and the Bankruptcy Act; * * *. We therefore see no reason why the language employed in *Mayer v. Hellman* to meet the claim there made, as here, that the Bankruptcy Act suspended the 'operation of the act of Ohio regulating the mode of administering assignments,' is not quite as applicable now as it was then. * * *. It follows that the present deed of assignment is valid, both as respects the common law and the statutes of Ohio."

§ 1633. **Various Holdings as to What Amount to "Insolvency" Proceedings.**—There are various holdings as to what amount to insolvency proceedings.

Thus, a proceedings in the form of a creditor's bill, filed under §§ 2716-2722, Code of Georgia, with the averments and prayers essential under those sections, is an insolvency or state bankruptcy proceedings.⁴²

Carling v. Seymour Lumber Co., 8 A. B. R. 35, 113 Fed. 483 (C. C. A. Ga., reversing on other grounds *In re Macon Lumber Co.*, 7 A. B. R. 66, 112 Fed. 322): "These sections, in brief, provide that when any corporation not municipal, or any trader being insolvent, fails to pay debts at maturity, creditors representing one-third or more of the unsecured debts of the insolvent may invoke by petition the power of a court of equity to collect the debts and distribute the assets of such insolvent. The chancellor is authorized, in cases where the insolvent has fairly surrendered his property for distribution, 'to recommend to the creditors of the defendant that they may release him from further liability.' This insolvent traders' act is held by the Supreme Court of Georgia to be a kind of state bankrupt law. Describing the procedure, the court said: 'It is putting a trader in bankruptcy, and relieving him from past debts, as far as state legislation can do so.' *Comer v. Coates*, '69 Ga. 491-495. In a later case this language is repeated and approved, and the court added: 'The act does in many respects resemble the bankruptcy acts of congress.'"

Likewise under the Arkansas statute.

In re Weedman Stave Co., 29 A. B. R. 460, 199 Fed. 948 (D. C. Ark.): "What constitutes an insolvency law? The elements of an insolvency law are insolvency, surrender of property, its administration by a receiver or trustee, distribution of the assets among the creditors, and a provision for priorities or other matters not permissible in the absence of such a statute. A provision for the discharge of the debtor from the unpaid balance of his debts is not essential to make it an insolvency law."

So, also, under West Virginia⁴³ and Pennsylvania⁴⁴ Law; although it

⁴². *In re Macon Lumber Co.*, 7 A. B. R. 66, 112 Fed. 322 (D. C. Ga., reversed, on other grounds, sub nom. *Carling v. Seymour Lumber Co.*, 8 A. B. R. 29, 113 Fed. 483, C. C. A. Ga.); *In re Allison Lumber Co.*, 14 A. B. R. 79, 137 Fed. 643 (D. C. Ga.); *In re Pickens Mfg. Co.*, 20 A. B. R. 202, 166

Fed. 585 (D. C. Ga.).

⁴³. Compare, to same general effect, inferentially, *In re Porterfield*, 15 A. B. R. 11, 138 Fed. 192 (D. C. W. Va.).

⁴⁴. *In re International Coal Min. Co.*, 16 A. B. R. 311, 142 Fed. 665 (D. C. Penn.).

has also been held that the Pennsylvania statute of July 12, 1842, is not an insolvency statute, but merely a proceedings in aid of execution, and therefore not ipso facto suspended by the Bankruptcy Act.⁴⁵

In re Crawford, 18 A. B. R. 618, 154 Fed. 769 (C. C. A. Pa., affirming *Johnson v. Crawford*, 18 A. B. R. 608, 154 Fed. 761, C. C. Pa.): "The Pennsylvania statute of July 12, 1842, is not an insolvent law. The proceeding it provides is not designed to effect the distribution of the debtor's assets among his creditors. It is a proceeding in aid of execution. Its object is to reach property of the judgment debtor which he fraudulently conceals."

But if the proceedings may also operate as a mere suit in equity to foreclose a pre-existing and valid mortgage lien, it will not be superseded because of its being able also to operate as a proceedings under a state insolvency statute; and this is so, although, as incident thereto, a receiver is appointed to preserve the mortgaged assets.⁴⁶

Thus, in some instances general assignments under state statutes have been declared to be in effect general insolvency laws,⁴⁷ but in other instances, general assignments for the benefit of all creditors who will accept and release the debtor have been held not to be so.⁴⁸

§ 1634. Receiverships and Winding Up of Insolvent Corporations, Whether Insolvency Proceedings.—Certain receiverships under state law have sometimes been held to amount to state insolvency proceedings and as such to be superseded by bankruptcy.⁴⁹

Thus, also, proceedings in state courts for the dissolution and winding up of insolvent corporations have been held to be in the nature of insolvency proceedings and to be subject to the rule that they are suspended by the Federal Bankrupt Act.⁵⁰

45. *Johnson v. Crawford*, 18 A. B. R. 608, 154 Fed. 761 (C. C. Pa., affirmed sub nom. In re Crawford, 18 A. B. R. 618, 154 Fed. 769, C. C. A. Pa.).

46. *Carling v. Seymour Lumber Co.*, 8 A. B. R. 29, 113 Fed. 483 (C. C. A. Ga., reversing In re Macon Lumber Co., 7 A. B. R. 66, 112 Fed. 322, D. C. Ga.).

47. In re Curtis, 1 A. B. R. 440, 91 Fed. 737 (D. C. Ill.); In re Smith & Dodson, 2 A. B. R. 9 (D. C. Ind.).

48. *Patty-Joiner Co. v. Cummins*, 4 A. B. R. 269, 57 S. W. 566, 93 Tex. 598; also [1867] *Boese v. King*, 108 U. S. 379.

49. *Obiter*, In re Kersten, 6 A. B. R. 519, 110 Fed. 929 (D. C. Wis.).

Compare, In re Electric Supply Co., 23 A. B. R. 647, 175 Fed. 612 (D. C. Ga.), although the decision is not based on the ground that such proceedings amount to insolvency pro-

ceedings under an insolvency law superseded by the Bankruptcy Act.

50. In re International Coal Min. Co., 16 A. B. R. 311, 143 Fed. 655 (D. C. Pa., affirmed sub nom. *Coal & Coke Co. v. Stauffer*, 17 A. B. R. 573, 148 Fed. 981, C. C. A. Penn.). Even though no receiver nor trustee is appointed, but merely the sheriff acts.

In re Storck Lumber Co., 8 A. B. R. 86, 114 Fed. 860 (D. C. Md.). Compare, apparently to same effect, In re Watts, 10 A. B. R. 113, 190 U. S. 1; In re Lengert Wagon Co., 6 A. B. R. 535, 110 Fed. 927 (D. C. N. Y.). Compare, as act of bankruptcy. In re Milbury Co., 11 A. B. R. 523 (D. C. N. Y.). Compare (but not void until bankruptcy), *Ex rel Strohl v. Sup. Ct. King's Co.*, 2 A. B. R. 92 (Sup. Ct. Wash.).

Compare, In re Electric Supply Co., 23 A. B. R. 647, 175 Fed. 612 (D. C. Ga.).

Mauran v. Carpet Lin. Co., 6 A. B. R. 734, 50 Atl. 331 (R. I.): "The proceeding in the State court against the Crown Carpet Lining Company, resulting in the appointment of a receiver, was practically an insolvency proceeding."

Thus, proceedings under state statutes to wind up and liquidate insolvent private banks have been held to amount to state insolvency proceedings and not to be within any exception on account of being an exercise of the police power.⁵¹

On the other hand fraudulent conveyance suits instituted by a receiver of a judgment debtor have been held not to amount to insolvency proceedings;⁵² likewise, fraudulent conveyance suits instituted by creditors without judgment, under favor of state statute.⁵³ And suits under state statutes to set aside preferential transfers have been held not to be insolvency proceedings within the meaning of the law superseding insolvency proceedings by bankruptcy proceedings.⁵⁴

So, a state law for the regulation of building and loan associations whereby their business might be discontinued and their affairs wound up, when found to be in an unsafe condition, has been held to be enforceable in the state courts in so far as such enforcement does not conflict with the due administration of the bankruptcy act.⁵⁵

§ 1635. Procedure to Procure Surrender from State Bankruptcy or Insolvency Courts.—The same rules as to the method of procedure prevail in regard to obtaining surrender or possession where the state court has custody under state bankruptcy or state insolvency proceedings, as in cases of nullified assignments, receiverships, etc., under state laws not amounting to state bankruptcy or state insolvency laws.⁵⁶

§ 1636. Thus, State Court Receiver May Be Enjoined.—Thus, injunctions may issue to restrain the proceedings in the state court.

Carling v. Seymour Lumber Co., 8 A. B. R. 41, 113 Fed. 483 (C. C. A. Ga.): "The jurisdiction and authority of the bankruptcy court for the enforcement of the Bankrupt Law is paramount. State insolvency laws are superseded by the Bankrupt Act. While it is a general rule that a Federal court may not enjoin proceedings in a State court, an exception is made in cases where such injunction may be authorized by any law relating to proceedings in bankruptcy. Rev. Stat., U. S., § 720. When the State court is in possession, through its receiver, of assets that it is without jurisdiction or authority to hold against a receiver or trustee appointed in bankruptcy proceedings, instead of making a peremptory order on the receiver of the State court to surrender the funds, an

51. In *re Salmon & Salmon*, 16 A. B. R. 132, 143 Fed. 395 (D. C. Mo.).

52. In *re Meyers & Co.*, 1 A. B. R. 347 (Ref. N. Y.).

53. *Grunsfeld Bros. v. Brownell*, 11 A. B. R. 599, 12 N. Mex. 192.

54. *Grunsfeld Bros. v. Brownell*, 11 A. B. R. 599, 12 N. Mex. 192.

55. *Continental, etc., Assoc. v. Su-*

perior Court, 28 A. B. R. 873, 163 Cal. 579.

56. See cases cited under same rule relative to the custody of state officers under nullified legal liens, ante, § 1601, and post, § 1830: under void assignments and receiverships, ante, § 1611: and on the general subject of Summary Orders on Court Officers in possession, § 1860.

injunction, if necessary, might be granted by the bankruptcy court to prevent the unlawful distribution of the assets, until application could be made to the State court for an order to its receiver to surrender the assets to the proper custodian. The laws of the United States being equally binding on all the courts, we cannot assume that the State court would refuse to administer them. We are not now called on to decide what course should be taken in the event of a disregard of the Bankrupt Law by the State court. That such application should be made in the first instance to the State court is sustained, not only by the analogous cases relating to comity, but by adjudication directly in point on this question of practice under the Bankrupt Law."

§ 1637. **Comity Requires Resort First to State Tribunal.**—Thus, likewise, comity requires resort first to the tribunal of the state court for an order of surrender.⁵⁷

And this principle has been applied even in the case of a state trust company which was a designated depository for the money of bankrupt estates, and which failed and was placed in charge of the state superintendent of banks.

In *re Bologh*, 25 A. B. R. 726, 185 Fed. 825 (D. C. N. Y.): "It is argued that the court in designating a depository in which a receiver is required to deposit that portion of the assets which consists of money in effect appoints two custodians, one the receiver, who is to act as a custodian of the assets other than cash, and the other a trust company, which is to act as a custodian of the cash, and that therefore any trust company designated as a depository is subject to the summary order of the court in the same manner as a receiver. This suggestion seems to me unsound. A receiver or other officer of the court who deposits money in a trust company, in my opinion, simply creates thereby the same relation of debtor and creditor as is created by any bank deposit. The debt may have a preference, but it is nevertheless a debt, and I do not think that the bankruptcy court can exercise the same summary authority over such a depository that it can over a receiver. If the trust company is appointed directly a receiver, then the bankruptcy court can undoubtedly, so long as the trust company continues to conduct its business as a solvent institution, exercise the same immediate control over it that it can over other receivers; but when it simply acts as a depository for receivers' funds it seems to me that even when the trust company is conducting its business in the ordinary way the court has no summary jurisdiction over it. But in any event, when a trust company has ceased to conduct its business and its property has been taken possession of by an officer authorized to liquidate its affairs, I think it clear that a court of bankruptcy cannot by a summary order direct that the bankruptcy funds deposited with it shall be paid over. If such a power existed bankruptcy receivers and trustees might obtain a preference over other preferred creditors under the statute. If a trust company had been appointed directly a receiver or a trustee, and had become insolvent and its assets had been taken possession of by an officer authorized to wind up the institution, I do not think that in that case the court could order the funds turned over by a summary order

⁵⁷. *Carling v. Seymour Lumber Co.*, 8 A. B. R. 29, 113 Fed. 483 (C. C. A. Ga.): *Hooks v. Aldridge*, 16 A. B. R. 664, 145 Fed. 865 (C. C. A. Tex.).

See also cases cited under same rule as applicable to the custody of State

officers under nullified legal proceedings, ante, § 1601, and post, § 1830; void assignments and receiverships, ante, § 1611; and summary orders on custodians, post, § 1860.

in the same manner in which it could make such an order if the company had remained solvent. When the insolvency of a corporation occurs, or any such condition arises that the law authorizes an officer to step in and stop the business and take possession of the property for the purposes of liquidation, the status is completely changed, and the officer who succeeds to the possession of the assets is not subject to the same control or to be proceeded against in the same summary manner as the company was in its capacity and as officer of the court so long as it continued in business."

And the resort first to the State court is not such an election of forum, nor is an adverse ruling there such a *res judicata*, as to preclude the subsequent issuance of a restraining order by the bankruptcy court.⁵⁸

Whenever the state court surrenders the assets, the validity and extent of any lien thereon in favor of the insolvency officers must be left to the bankruptcy court for determination, and there is no jurisdiction in the state court to fix the same, and any order to that effect will be disregarded;⁵⁹ although the rule might be different in cases of the superseding of assignees and receivers in other than state insolvency or state bankruptcy proceedings, since such proceedings are not absolutely void.⁶⁰

DIVISION 4.

VOLUNTARY SURRENDER OF CUSTODY BY STATE COURT.

§ 1638. Voluntary Surrender by State Court.—If the state court voluntarily surrenders possession it is divested of jurisdiction, and the bankruptcy court is invested therewith.

In *re American, etc., Co.*, 25 A. B. R. 651, 184 Fed. 694 (C. C. A. Ohio): "The reason why the bankruptcy court would refrain from interfering with the proceedings in a state court and anticipate its judgment is the obligation of the comity necessary to be observed to avoid conflict between the state and federal courts, and this reason would be wanting if the other court waives its priority of right to possession."

In *re Hymes Buggy & Implement Co.*, 12 A. B. R. 477, 130 Fed. 577 (D. C. Mo.): "But passing this by, it affirmatively appears from the referee's findings, and the evidence amply sustains it, that whatever possession of the goods the sheriff acquired under the writ of replevin was on the 4th day of May, 1904, voluntarily surrendered by him to the receiver in bankruptcy. This constituted an abandonment of his seizure, and entitled the receiver in bankruptcy, as the representative *pro hac* of the debtor and creditors, to receive and to hold it. It is a well-settled rule of law that a release of the goods levied on or seized under writ by a sheriff is an abandonment thereof, and invalidates the levy."

58. In *re Bologh*, 25 A. B. R. 726, 185 Fed. 825 (D. C. N. Y.).

59. In *re Rogers*, 8 A. B. R. 723, 116 Fed. 435 (D. C. Ga.); *Carling v. Sey-*

mour Lumber Co., 8 A. B. R. 41, 113 Fed. 483 (C. C. A. Ga.); ante, § 1620.

60. See ante, § 1620.

SUBDIVISION "A."

PENDING SUITS BY AND AGAINST BANKRUPTS.

§ 1639. **Pending Suits against Bankrupt—Subrogation of Trustee to Creditor's Lien Where Lien Preserved.**—A trustee may be subrogated to the rights of the plaintiff and be substituted for him in pending actions, wherein a lien by legal proceedings has been obtained within four months, which would otherwise be nullified by the adjudication in bankruptcy, but which is preserved for the benefit of the estate.⁶¹

§ 1640. **Pending Suits by Bankrupt—Substitution of Trustee.**—The trustee may, with the approval of the court, be permitted to prosecute as trustee any suit commenced by the bankrupt prior to the adjudication, with like force and effect as though it had been commenced by him.⁶² He may, but need not, be permitted so to prosecute.⁶³

Kessler v. Herklotz, 22 A. B. R. 259, 132 N. Y. App. Div. 278: "We are of opinion, however, that the appellant is not liable for any part of the costs. He did not become a party to the action, and he did not accept the subject-matter of the litigation as an asset, nor did he intend to become in any manner responsible for the litigation without the authority of the Federal court, if that was necessary. It is well settled that the trustee in bankruptcy is not obliged to intervene in a pending action by or against the bankrupt. This is upon the ground that it may not be for the interests of the estate to make any claim on account of the matter in controversy and that the trustee in such circumstances may elect to abandon any claim thereto. *Fleming v. Courtenay*, 98 Me. 401; *Hahlo v. Cole*, 15 Am. B. R. 591, 112 App. Div. 636. All rights of action in favor of the bankrupt arising on contract vest in the trustee by virtue of the provisions of clause 6 of subdivision a of § 70, of the Federal Bankruptcy Act of 1898. * * * He may, however, allow them to proceed without intervention and accept the fruits if successful."

§ 1641. **Preliminary Order of Approval Proper.**—An order, signifying the court's approval, should, as a prerequisite, be entered by the referee, authorizing or directing the trustee to prosecute the suit.⁶⁴ The court which appointed the trustee is the court which may authorize him to intervene.⁶⁵

Such preliminary order is not requisite, however, where the trustee institutes the action himself and is not merely substituted for the bankrupt in an action already pending.⁶⁶

61. See for full discussion of the "Preservation of Nullified Legal Liens," ante, § 1489.

62. Bankr. Act, § 11 (c); (obiter) *Patten v. Carley*, 8 A. B. R. 482 (N. Y. Sup. Ct. App. Div.).

63. *Griffin v. Mut. Life Ins. Co. of N. Y.*, 11 A. B. R. 622, 119 Ga. 664; *Johnson v. Collier*, 27 A. B. R. 454, 222 U. S. 538.

64. Bankr. Act, § 11 (c); *In re Price*, 1 A. B. R. 606, 92 Fed. 987 (D. C. N.

Y.); *Hahlo v. Cohn*, 15 A. B. R. 591, 112 N. Y. App. Div. 636; impliedly, *Traders' Ins. Co. v. Mann*, 11 A. B. R. 272 (Sup. Ct. Ga.); impliedly, *Callahan v. Israel*, 186 Mass. 383; *Bear v. Chase*, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S. C.). See ante, § 899. *Kessler v. Herklotz*, 22 A. B. R. 257, 132 N. Y. App. Div. 278.

65. *Malloch v. Adams*, 28 A. B. R. 916, 199 Fed. 542 (D. C. Mass.).

66. *Hahlo v. Cohn*, 15 A. B. R. 591,

§ 1642. **Probability of Success Should Appear.**—Probability of success, not certainty of it, is all that is necessary to show in the application for such an order; or, if a proposition of settlement has been made, that more could probably be obtained by the suit than by the settlement.⁶⁷

The trustee will not be ordered to defend a suit wherein success is doubtful, against the wishes of a majority of the creditors, unless the minority creditors desiring him to do so shall indemnify the estate against costs and expenses.⁶⁸

§ 1643. **Only Suits on Rights Passing to Trustee Authorized.**—Only such suits will be authorized to be prosecuted as are founded on rights of action that would pass to the trustee in bankruptcy.⁶⁹

Thus, the court would not authorize the trustee to prosecute a slander suit, or a suit for malicious prosecution, begun by the bankrupt before adjudication.⁷⁰ Nor will substitution be permitted in an action for libel.⁷²

It has been held that, after judgment has been entered in a local court against a bankrupt plaintiff for costs, if the trustee is permitted to intervene at all it will only be for the purpose of prosecuting an appeal; such intervention, it was held, will not be allowed where the only purpose and effect of it would be to relieve the plaintiff from the judgment or costs.⁷³

Thus, the liability of stockholders for unpaid stock subscriptions in a bankrupt corporation the trustee will be ordered to enforce by appropriate action.⁷⁴

§ 1644. **Defendant Not Released by Failure of Trustee to Assume Prosecution.**—If the trustee does not take up the prosecution of the suit, the defendant is not released, even where the right of action is one that might have passed to the trustee; but the bankrupt may continue the prosecution.⁷⁵

Hahlo v. Cohn, 15 A. B. R. 593 (Sup. Ct. N. Y.): "An action by or against the bankrupt in the State Court does not abate upon the adjudication in bankruptcy or appointment of a trustee, and in the absence of an application by the trustee for substitution it may be prosecuted or defended by the bankrupt."

He is interested in the fund, either as the source of his exemptions, or as a means of enlarging the estate for his creditors.⁷⁶ And this is so, even

112 N. Y. App. Div. 636; *Traders Ins. Co. v. Mann*, 11 A. B. R. 272 (Sup. Ct. Ga.); *Callahan v. Isreal*, 186 Mass. 383; contra, obiter, *In re Ryburn*, 16 A. B. R. 515, 145 Fed. 662 (D. C. Conn.); *Kessler v. Herklotz*, 22 A. B. R. 257, 132 N. Y. App. Div. 278; also, see ante, § 899.

67. *In re Phelps*, 3 A. B. R. 396 (Ref. N. Y.).

68. *In re Kearney Bros.*, 25 A. B. R. 757, 184 Fed. 190 (D. C. N. Y.).

69. See § 1020. *In re Haensell*, 1 A. B. R. 286, 91 Fed. 355 (D. C. Calif.); inferentially, *In re Price*, 1 A. B. R.

606, 92 Fed. 987 (D. C. N. Y.).

70. *In re Haensell*, 1 A. B. R. 286, 91 Fed. 355 (D. C. Calif.).

72. *Epstein v. Handwerker*, 26 A. B. R. 712, 29 Okla. 337.

73. *Murtaugh v. Sullivan*, 27 A. B. R. 431 (Sup. Ct. N. Y.).

74. See ante, "Unpaid Stock Subscriptions as Assets," § 976.

75. *Griffin v. Mut. Life Ins. Co.*, of N. Y., 11 A. B. R. 622, 119 Ga. 664.

76. *Griffin v. Mut. Life Ins. Co.* of N. Y., 11 A. B. R. 622, 119 Ga. 664. But compare, *In re Levy*, 7 A. B. R. 56 (Ref. N. Y.).

though no trustee were appointed.⁷⁷ And the bankrupt need not get leave from the bankruptcy court to continue the suit, at any rate where the right of action could not, in any event, have passed to the trustee.⁷⁸

§ 1645. **Ordering Trustee to Apply for Leave to Defend.**—The bankruptcy court may order the trustee to apply for leave to enter his appearance and to defend any pending suit against the bankrupt.⁷⁹

§ 1646. **Intervening Not Usually Proper Except Where Property Involved.**—Here, again, the touchstone is whether any property of the creditors in bankruptcy is involved.⁸⁰ If the suit is a foreclosure suit, or a creditor's bill, or replevin⁸¹ or other suit affecting the property of the bankrupt, of course it will be proper for the trustee to defend and prove the invalidity of the liens, or reduce their amount, or prove right of property; for thus he will increase the assets of the estate.⁸²

The trustee may be required to respond to garnishment proceedings pending at the time of bankruptcy, wherein the bankrupt was garnishee; but only to the extent of dividends, and only by order of the bankruptcy court. And the garnishment proceedings may be stayed until the dividends can be ascertained.⁸³

Again, the trustee may be interested in a pending suit against the bankrupt for infringement of a patent.⁸⁴

§ 1647. **Intervening in Suits in Personam.**—The court would hardly order the trustee to defend a suit in personam against the bankrupt, for such suit ordinarily would not affect the rights of the creditors. Yet, inasmuch as it is possible for judgments obtained after bankruptcy but before discharge to be proved (§ 63 (5)), occasion will arise when it will be to the creditors' interest to have the trustee defend even a suit merely in personam. Especially is this so where the bankruptcy court itself has ordered that a pending suit be maintained as a method of liquidating an unliquidated demand, under § 63 (b).⁸⁵

77. *Griffin v. Mut. Life Ins. Co. of N. Y.*, 11 A. B. R. 622, 119 Ga. 664.

78. *In re Haensell*, 1 A. B. R. 286, 91 Fed. 355 (D. C. Calif.).

79. Bankr. Act, § 11 (b): "The court may order the trustee to enter his appearance and defend any pending suit against the bankrupt." *Obiter*, *Patten v. Carley*, 8 A. B. R. 482, 69 N. Y. App. Div. 423.

80. *In re St. Alban's Fdy. Co.*, 4 A. B. R. 594 (D. C. Vt.); impliedly, *In re Klein*, 3 A. B. R. 174, 97 Fed. 31 (D. C. Ills.).

But compare erroneous decision *In re Rogers*, 1 A. B. R. 541 (Ref. Ky.), where the court undertook to stay proceedings and to get possession of property acquired subsequently to bank-

ruptcy for the benefit of a creditor whose claim was not dischargeable.

81. Inferentially, *In re Neely*, 7 A. B. R. 312, 113 Fed. 210 (C. C. A. N. Y.).

82. *Heath v. Shaffer*, 2 A. B. R. 98, 93 Fed. 647 (D. C. Iowa).

And the bankruptcy court may restrain the proceedings in the State court to give time for the trustee in bankruptcy to intervene, *In re Klein*, 3 A. B. R. 174, 97 Fed. 31 (D. C. Ills.).

83. *In re The St. Albans Fdy. Co.*, 4 A. B. R. 594 (D. C. Vt.).

84. *Victor Talking Mach. Co. v. Hawthorne*, 23 A. B. R. 234, 173 Fed. 617 (U. S. C. C. Pa.), quoted at § 1779.

85. *In re Simon*, 3 N. B. N. & R. 807 (Ref. Ohio). Compare, *In re Johnson*, 11 A. B. R. 544 (D. C. Nev.), where the State court was permitted

§ 1648. State Court Governed by State Law and Judicial Policy in Granting or Refusing Application.—The state court will be governed in deciding the application, by state laws and judicial policy.⁸⁶

Bank of Commerce v. Elliott, 6 A. B. R. 409, 109 Wis. 648: "Counsel insists that because § 11 (b) of the Bankruptcy Act provides that in a proceeding under it, the Federal Court may order the trustee to enter his appearance and defend any pending suit against the bankrupt, and the trustee in the matter of Elliott's bankruptcy was so ordered, the Circuit Court having the garnishee actions in question in charge was found to give effect to such order by granting the motion to make him a party to such actions. That subject was before this court and was fully considered in *Distilling Co. v. Seidel*, 103 Wis. 489, 79 N. W. 744. We there held, and now affirm, that the Federal statute, however mandatory its terms, does not control the practice in State courts, and was not intended to do so. If an order be made under it commanding a trustee to intervene in the State court in an action to which the bankrupt is a party, the former performs his full duty when he makes a proper application to such court to be let in to such action. In disposing of such application the statutes of the State, and the rules and practice of its court, must necessarily govern, the same as when any other party invokes the court's jurisdiction.

"Testing the ruling of the court, refusing to make the trustee in bankruptcy a party to the garnishee actions, by State laws and judicial policy, we fail to see why the trustee had any interest in the action that required his presence therein for his due protection, or why the entire controversy in such action, as to the plaintiff, was not susceptible of a complete determination without the trustee being brought in. Therefore, § 2610, Rev. St. 1898, did not require the trial court to grant the motion, but left it free to exercise its discretion in respect thereto. If we say plaintiff acquired a right, by the commencement of the garnishee action, to hold the garnishee liable for some part of its indebtedness to Elliott, and that such right, by operation of law, was displaced by the right of the trustee in bankruptcy so as to bring the latter within the scope of § 2801, *id.*, then it would follow that the action of the trial court could not be disturbed unless it clearly appeared that there was an abuse of judicial discretion. Granting or refusing a motion under that section is, by its terms, addressed to the sound discretion of the court. In any event, since, as will be hereafter seen, there was no controversy between the trustee and appellant as to who should have the benefit of the liability of the garnishee to Elliott, appellant was not prejudiced by the denial of the motion to make the trustee a party, and cannot be heard to complain of such denial on this appeal. Section 2829, *id.*

"Again, regardless of the rights of the trustee under section 2901, Rev. St. 1898, appellant has no standing here to recover on the assignment of error under discussion, because the privilege was one to be asserted by the trustee. He did not appear in the court below and ask to be made a party, as we understand the record, nor is he a party to the appeal."

to determine the validity of a lien on property in the bankruptcy court's custody and to make the trustee a party defendant.

⁸⁶ Compare, *In re Price*, 1 A. B. R. 606, 92 Fed. 987 (D. C. N. Y.). Instance, *Murtaugh v. Sullivan*, 27 A. B. R. 431 (Sup. Ct. N. Y.).

If such an application to intervene

is denied, only a party aggrieved by the adverse decision can be heard on appeal therefrom; and the trustee can not be so heard unless he shall first have applied to the State court, failed in his application and appealed specially from the decision, *Bank of Commerce v. Elliott*, 6 A. B. R. 409 (Sup. Ct. Wis.).

By intervening, the trustee does not oust the state court of jurisdiction, although the trustee claims the transfer involved is a preferential transfer given within four months of the bankruptcy.

Savings Bk. v. Jewelry Co., 12 A. B. R. 781, 123 Iowa 432: "That the enactment of a general bankruptcy law so far supersedes and suspends the operation of State insolvency laws as that a receiver or assignee in insolvency proceedings instituted under State statutes may be properly required to surrender possession to a trustee in bankruptcy, may be conceded. And such are the cases cited by counsel for appellant. But such doctrine cannot be extended to an action for the enforcement of a specific lien. Jurisdiction of such actions in the State court is not sought to be taken away by the Federal statute, and such could not well be. The action is not one to administer upon the estate of the bankrupt, or any portion of such estate. The purpose thereof is to ascertain if the plaintiff have a right to resort, by virtue of a specific lien claim, to the particular property in controversy, as against all other creditors or claimants, for the payment of his debt or the satisfaction of his demand. His rights would be the same whether presented to the State or the Federal court in an action to foreclose, or by way of a claim made in the bankruptcy proceedings. Hence it is that the court which first takes jurisdiction and assumes control of the property retains it for all the purposes of a final order or decree. True, the trustee in bankruptcy may intervene in such action pending in the State court, as did this intervener, and be heard to contest the existence or the validity of the specific lien claimed, and he may well be awarded the property in the event the existence of the lien claimed is denied by the decree. But that a trustee may work an ouster of jurisdiction in the State court in such cases by pointing out the pendency of the bankruptcy proceedings has no support in reason or well-considered authority."

§ 1649. **Manner of Intervention.**—The intervention may be by way of substitution of the trustee for the bankrupt.⁸⁷

The trustee may limit his application to certain objects.

Bear v. Chase, 3 A. B. R. 746, 757, 99 Fed. 920 (C. C. A. S. C.): "Such petition should have been limited to a request to transfer the money to the Bankrupt Court."

The application, in the first instance at least, should be made to the court where the action is pending and which has power to protect the other party by the imposition of proper conditions.⁸⁸

§ 1650. **Trustee Bound as Any Other Litigant, on Intervention.**—When the trustee is substituted for the bankrupt, his submission to the jurisdiction binds him to the judgment rendered, subject only to his rights as a litigant in the state courts.⁸⁹ But he incurs no liability for costs ac-

⁸⁷. *Obiter*, and inferentially, *Griffin v. Mut. Life Ins. Co.*, 11 A. B. R. 623, 119 Ga. 664.

⁸⁸. *Murtaugh v. Sullivan*, 27 A. B. R. 431 (Sup. Ct. N. Y.).

⁸⁹. *Savings Bk. v. Jewelry Co.*, 12 A. B. R. 781, 123 Iowa 432.

Obiter, *In re Neely*, 7 A. B. R. 312, 113 Fed. 210 (C. C. A. N. Y.), which

was a replevin case, in which the court held the trustee bound for costs.

In re Van Alstyne, 4 A. B. R. 42, 100 Fed. 929 (D. C. N. Y.), which was a case of foreclosure of mechanic's lien. Inferentially, *Bank of Commerce v. Elliott*, 6 A. B. R. 409 (Sup. Ct. Wis.).

Not liable for costs where he does not intervene, though case prosecuted

cruing prior to his intervention; nor will he become personally liable for any costs, providing of course, he acts in good faith.⁹⁰

§ 1650½. **Making Trustee Party Defendant.**—Conversely, the trustee may, on proper application and in a proper case, be made a party defendant in a suit by another.⁹¹

§ 1651. **Stay of Pending Suits.**—The subject of the stay of pending suits is considered elsewhere. So far as such stay is for the benefit of the bankrupt, to give him opportunity to secure his discharge and present it as a defense in bar, it is discussed under the general subject of discharge.⁹² So far as such stay is for the benefit of the estate, it is considered under the various subjects of injunctions and restraining orders.⁹³

by creditors with his acquiescence.
Kessler v. Herklotz, 22 A. B. R. 257
278 N. Y. App. Div. 132.

90. Mallach v. Adams, 28 A. B. R.
916, 199 Fed. 542 (D. C. Mass.).

91. See post, § 1779, et seq.

92. See post, § 268C, et seq.

93. See ante, § 359, et seq.; post, §
1901, et seq.

CHAPTER XXXIII.

JURISDICTION OVER ADVERSE CLAIMANTS.

Synopsis of Chapter.

- § 1652. Jurisdiction over "Adverse Claimants."
- § 1653. Before Amendment of 1903 Neither Summary nor Plenary Jurisdiction over Adverse Claimants Existed in Bankruptcy Court.
- § 1654. Injunctions on Adverse Claimants Issuable in Bankruptcy Proceedings.
- § 1654½. Whether "Adverse Claimant in Possession" Determined by Pleadings.

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- § 1655. "Adverse Claimant" Not Confined to Absolute Owners.
- § 1656. Adverse Claimant and Bankrupt Holding Jointly, Bankruptcy Court Has Jurisdiction.
- § 1657. Adverse Claimant Obtaining Voluntary Possession from Bankruptcy Officer, Not Subject to Summary Jurisdiction.
- § 1657½. Creditors Receiving Property after Filing of Petition, Not "Adverse" When.
- § 1658. Adverse Claimant Himself Becoming Bankrupt Gives Jurisdiction.
- § 1659. Attaching Creditor Receiving Proceeds, within Four Months, Adverse Claimant.
- § 1660. Receiving Proceeds after Bankruptcy, Not "Adverse Claimant."
- § 1661. Proceeds Still in Officer's Hands; Neither Creditor nor Officer Adverse Claimant.
- § 1662. Court Officers in Possession, Adverse Claimants until Adjudication.
- § 1663. Whether Garnishee Adverse Claimant Where Garnishment within Four Months.
- § 1664. Wife "Adverse Claimant" as to Property She May Hold Adversely to Husband.
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- § 1667. Agent in Possession Applying Funds on Salary.
- § 1668. Trustee in Possession under Mortgage for Benefit of Certain Creditors, "Adverse Claimant."
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- § 1670. Executor Holding Legacy to Bankrupt, Not "Adverse Claimant."
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- § 1677. Alleged Preferential Transferee in Possession, "Adverse Claimant."

- § 1678. Assignee of Bankrupt's Wages, "Adverse Claimant."
- § 1679. Lienholder and Secured Creditor as "Adverse Claimants."
- § 1680. Debtors of Bankrupt "Adverse Claimants," Not to Be Proceeded against Summarily.
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- § 1682. Likewise, Owner Owing on Building Contract, Subject to Mechanic's Liens, "Adverse Claimant."
- § 1683. Also, Employers Holding Wages of Bankrupt Tied Up by Assignment, "Adverse Claimants."
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- § 1684. Plenary Suits against "Adverse Claimants" in State Courts.
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§ 1652. Jurisdiction over "Adverse Claimants."—Third parties having at the time of the bankruptcy possession of the tangible property or funds involved, under claim of a beneficial or adverse interest therein, cannot be obliged to surrender them, nor can third parties owing debts to the bankrupt at the time of the bankruptcy, be obliged to pay the debts, nor can such parties be obliged to submit their rights in such property, funds or debts for deter-

mination to the bankruptcy court, by summary proceedings in the bankruptcy proceedings, even on notice and hearing: Such property, funds or debts thus owed or adversely held, are to be reached only by instituting plenary suits, in which the parties may be brought into court by due service of summons or subpoena, pleadings may be filed, issues joined and trial had, in accordance with the usual forms of procedure.¹

Obiter, Bardes v. Bank, 178 U. S. 524, 4 A. B. R. 163: "It was also repeatedly held by this Court that the right of an assignee in bankruptcy to assert a title in property transferred by the bankrupt before the bankruptcy to a third person,

1. Compare cases cited under the subject of summary jurisdiction over bankrupts and others, post, §§ 1794 and 1795.

Beach v. Macon Grocery Co., 8 A. B. R. 751, 116 Fed. 143 (C. C. A.); *In re Rockwood*, 1 A. B. R. 272, 91 Fed. 363 (D. C. Iowa); *In re Kelly*, 1 A. B. R. 306, 91 Fed. 504 (D. C. Tenn.); *In re Flynn & Co.*, 11 A. B. R. 318, 126 Fed. 422 (D. C. N. Car.); *In re Scherber*, 12 A. B. R. 616, 131 Fed. 121 (D. C. Mass.); *Hinds v. Moore*, 14 A. B. R. 1, 134 Fed. 221 (C. C. A. Tenn., reversing *In re Leeds Woolen Mill Co.*, 12 A. B. R. 136, 129 Fed. 922); *Goodnough Mercantile & Stock Co. v. Galloway*, 19 A. B. R. 244, 156 Fed. 504 (D. C. Ore.); *In re Eurich's Fort Hamilton Brew.*, 19 A. B. R. 798, 158 Fed. 644 (D. C. N. Y.); compare, impliedly, *In re Darlington*, 20 A. B. R. 805, 163 Fed. 389 (D. C. N. Y.); *Mound Mines Co. v. Hawthorne*, 23 A. B. R. 242, 173 Fed. 882 (C. C. A. Colo.), quoted at § 1796; *obiter, In re Driggs*, 22 A. B. R. 621, 171 Fed. 897 (D. C. N. Y.), quoted at § 1678; *Babbitt v. Dutcher*, 216 U. S. 102, 23 A. B. R. 519, quoted at § 1796; *In re Zotti*, 23 A. B. R. 812, 178 Fed. 304 (D. C. N. Y., reversing 23 A. B. R. 601), quoted at § 1681; *In re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.); *In re Gill*, 26 A. B. R. 883, 190 Fed. 726 (C. C. A.); *Bear Gulch, etc., Co. v. Walsh*, 28 A. B. R. 724, 198 Fed. 351 (D. C. Mont.); *In re Big Cahaba Coal Co.*, 26 A. B. R. 910, 190 Fed. 900 (D. C. Ala.); *First Natl. Bank v. Hopkins*, 29 A. B. R. 434, 199 Fed. 873 (C. C. A. Ga.); *In re Boston-Cerrillos Mines Corporation*, 30 A. B. R. 739, 206 Fed. 794 (D. C. N. Mex.); *In re Auerbach*, 29 A. B. R. 791, 202 Fed. 192 (C. C. A. N. Y.); *In re Bacon*, 28 A. B. R. 565, 196 Fed. 986 (D. C. N. Y.); *obiter, In re George A. Glenn*, 25 A. B. R. 806, 185 Fed. 554 (D. C. Pa.); *In re Rathman*, 25 A. B. R. 246, 183 Fed. 913 (C.

A. S. D.); *Johnston v. Spencer*, 27 A. B. R. 800, 195 Fed. 215 (C. C. A. Colo.); *In re Mimms and Parham*, 27 A. B. R. 469, 193 Fed. 276 (D. C. Ky.); *In re United Wireless Tel. Co.*, 27 A. B. R. 1, 192 Fed. 238 (D. C. N. J.); *In re Zotti*, 26 A. B. R. 234, 186 Fed. 84 (C. C. A. N. Y., affirming 23 A. B. R. 812, 178 Fed. 304).

Compare, where facts, however, are too meagrely stated in the report of the case, to settle the question of actual possession or control of the real estate involved. *In re Pickens & Bro.*, 26 A. B. R. 6, 184 Fed. 954 (D. C. Ga.).

In re Horgan, 21 A. B. R. 31, 164 Fed. 415 (C. C. A. Mass.). In this case sureties on a bail bond for the bankrupt were sustained in their objection to the jurisdiction of the court, to summarily order them to surrender moneys left with them as security where they claimed liens for expenses and for attorney's fees, though the liability on the bail was terminated by the court's exoneration of the bankrupt.

In re Buntrock Clothing Co., 1 A. B. R. 455, 457, 92 Fed. 886 (D. C. Iowa). This case was decided before the Amendment of 1903, and might have been decided on the broader grounds that no jurisdiction, either plenary or summary, existed, yet the decision was placed on the ground that the proceedings were summary; the court saying:

"* * * Upon their refusal to yield up possession thereof he obtained from the referee the issuance of an order directing them to show cause why they did not deliver up possession of the property to the trustee. * * * As is said by the Supreme Court in the case just cited (*Yeatman v. Inst.*, 95 U. S. 764), if the trustee questions the validity of the mortgages, he can attack the same by proper proceedings to that end, or he may redeem the property by payment of the mortgage liens, or in other ways may perhaps protect the

who now claimed it adversely to the assignee, could only be enforced by a plenary suit, at law or in equity, under the second section of the Act of 1867; and not by summary proceedings under the first section thereof, notwithstanding the declaration in that section that the jurisdiction in bankruptcy should extend 'to the collection of all the assets of the bankrupt,' and 'to all acts, matters and things to be done under and in virtue of the bankruptcy' until the close of the proceedings in bankruptcy. *Smith v. Mason* (1871), 14 Wall. 419; *Marshall v. Knox* (1872), 16 Wall. 551, 557; *Eyster v. Gaff* (1875), 91 U. S. 521, 525."

In *re Andre*, 13 A. B. R. 134, 135 Fed. 736 (C. C. A. N. Y.): "Prior to the decision in *Bardes v. Hawarden Bank*, * * * it was supposed by some of the Federal courts that pursuant to the provisions of § 23 of the Act, the bankruptcy courts had jurisdiction of all suits brought by trustees respecting property claimed to belong to the bankrupt's estate which was being administered by the trustee and which the bankrupt had transferred in contravention of the Act, and many of the courts which had adopted this construction of the section sanctioned the exercise by the bankruptcy courts of the power under §§ 2 and 69 to take such property into its custody for the preservation of the estate pending the appointment of the trustee, notwithstanding it was in the possession of some third person claiming an adverse title to it. The *Bardes* case decided that it was the intention of Congress, manifested by § 23, 'that controversies not strictly or properly part of the proceedings in bankruptcy, but independent suits brought by the trustee in bankruptcy, which assert a title to money or property as assets of a bankrupt against strangers to those proceedings should not come within the jurisdiction of the district courts of the United States 'unless by consent of the proposed defendant.' If Congress did not intend these controversies to be adjudicated by the bankruptcy courts, it cannot be reasonably supposed that Congress intended to permit the bankruptcy courts to adjudicate controversies respecting the title to the bankrupt's property with adverse claimants before the appointment of a trustee against the consent of the adverse claimant, and it would follow that the reasonable construction of the power con-

interests of creditors, but he can not by summary proceedings compel the delivery of possession of property by third parties, who hold the same as mortgagees, and whose possession antedates the filing of the proceedings in bankruptcy."

In *re Davis Tailoring Co.*, 16 A. B. R. 486, 144 Fed. 285 (D. C. N. J.); *inter alia*, *Horskins v. Sanderson*, 13 A. B. R. 102, 132 Fed. 415 (D. C. Vt.); *Publishing Co. v. Hutchinson Co.*, 17 A. B. R. 427 (Sup. Ct. Mich.).

Similarly, out of line with the great weight of authority is *In re Haupt Bros.*, 18 A. B. R. 585, 153 Fed. 239 (D. C. N. Y.), wherein the court (before adjudication), ordered the receiver to take summary possession of property in the hands of relatives of the bankrupt claiming to own it. The addendum of the court that "remedy here asked for is confessedly a most drastic one; it should not be used except in the clearest case and to prevent obvious loss through equally obvious fraud," hardly seems to lay down any

workable rule for exceptions to the well-established proposition that adverse claimants in possession are not to be proceeded against summarily, nor does it furnish an excuse for the creditors' or the receiver's failure to resort to the remedies which rightfully lay open to them. Similarly out of line with the authorities, appears to be the case *In re Nechamkus*, 19 A. B. R. 189, 153 Fed. 867 (D. C. N. Y.), wherein the court ordered a transferee of a horse to surrender it, though perhaps, in this case there was no objection raised to the jurisdiction; similarly out of line appears the obiter, *In re Berkowitz*, 22 A. B. R. 227, 173 Fed. 1012 (D. C. N. J.).

Contra, where the court sustained the referee in ordering seizure from the possession of an irresponsible vendee of the bankrupt's entire stock of goods. *In re Knopf*, 16 A. B. R. 432, 144 Fed. 245 (D. C. S. C.). This decision is out of line with the cases and cannot be brought into harmony with the great weight of authority.

ferred by § 2 and § 69 should be that it extends only to taking custody of property belonging to the bankrupt or which is in his possession or that a third person, as his bailee or agent, and not the property in the possession of an adverse claimant. This power must of course confer jurisdiction upon the bankruptcy court to ascertain whether the property is in the possession of the bankrupt or his bailee or agent, or whether it is in the possession of an adverse claimant and consequently to institute and entertain an appropriate proceeding for that purpose, and this proceeding must necessarily be a summary one, because as no trustee had been appointed there is no person to represent the estate as a party to a formal suit. Section 23 of the Bankrupt Act, as amended in 1903, confers jurisdiction upon the district courts without the consent of the defendant in suits for the recovery of property where the bankrupt has within a specified time made a preferential or fraudulent transfer of any of his property (subdivision b of § 60 and subdivision e of § 67). This amendment, however, cannot affect the original meaning of §§ 2 and 69, and the construction of these sections must remain as it was before. We conclude that it is only in cases in which the property of the bankrupt is in the possession of a party not an adverse claimant that the courts of bankruptcy have authority under these sections to interfere with it unless the adverse claimant chooses to consent, but that these courts have jurisdiction to entertain proceedings to ascertain whether there is an adverse claimant and that the mere refusal of a person in possession to surrender the property does not constitute him an adverse claimant."

In *re Grassler & Reichwald* (*Consani v. Brandon*), 18 A. B. R. 694, 154 Fed. 478 (C. C. A. Calif.): "The only question * * * is whether the proper remedy of the trustee to recover the money which was obtained by the petitioner was a plenary suit in court or a summary proceeding such as he adopted. If the property had been in the adverse possession of the petitioner [petitioner on review] before the bankrupts filed their petition to be adjudicated bankrupts there can be no doubt that a plenary suit would have been necessary. For further quotation, see post, § 1796. *Goodnough Mercantile & Stock Co. v. Galloway*, 19 A. B. R. 244, 156 Fed. 504 (D. C. Ore.).

Cooney v. Collins, 23 A. B. R. 840, 176 Fed. 189 (C. C. A. Montana): "John W. Cooney, by his verified answer not only claims the absolute right to hold all the property in question as against everybody, but specially alleges the reasons for his claim of ownership of it. Of course, his allegations in that behalf may not be true; still they make a case of adverse claim to the property on his part, to overcome which it was essential for the trustee to proceed in accordance with the provisions of § 23 of the Bankruptcy Act and not by summary proceedings in bankruptcy. We think the case of *Jaquith v. Rowley*, 188 U. S. 620, 9 Am. B. R. 525, is directly in point, on the authority of which the judgment of the District Court should be reversed, with directions to order the dismissal of the trustee's petition."

McNulty v. Feingold, 12 A. B. R. 338, 129 Fed. 1001 (D. C. Pa.): "The parties here have been adjudged bankrupts, a trustee appointed, and suit is instituted by him against third parties for the value of property fraudulently conveyed to them by the bankrupt. It is therefore a controversy at law or in equity, within the provision of § 23, and not a proceeding in bankruptcy, wherein summary proceeding can be had."

In *re Adams*, 12 A. B. R. 367, 130 Fed. 381 (D. C. R. I.): "As it is clear from the report of the referee, and from his decree, that Nash was, properly speaking, an adverse claimant, the referee, upon objection, should have declined to finally adjudicate the merits of the case on a summary petition."

In *re Teschmacher & Mrazay*, 11 A. B. R. 549, 127 Fed. 728 (D. C. Pa.): "As I understand the decisions of the Supreme Court in *Bardes v. Bank*, 178 U. S.

524, 4 A. B. R. 163; *Mueller v. Nugent*, 184 U. S. 1, 7 A. B. R. 224; *Louisville Trust Co. v. Comings*, 194 U. S. 18, 7 A. B. R. 421; *Jaquith v. Rowley*, 188 U. S. 620, 9 A. B. R. 525, and other decisions cited in those cases, a court of bankruptcy, before the amendments of 1903 were passed, had jurisdiction to inquire summarily upon petition and answer whether property alleged to belong to the bankrupt, but found in the possession of a third person when the petition was filed, was held by such person as the bankrupt's agent or mere representative; and in the exercise of this jurisdiction the court was of necessity empowered to inquire to some extent concerning the merits of the claim of title, or of a right to retain possession, that might be set up by the person in whose hands the property was found. If the result of the inquiry was to satisfy the court that a real adverse claimant existed—no matter how ill-supported it might appear to be—the court had no power to go further in that form of proceeding and decide summarily the question whether or not the claimant was entitled to prevail. It then became necessary, because the Bankrupt Act so declared, to remit the contestants to a plenary suit, either in a State court or in a Circuit Court of the United States, whichever might prove to be the appropriate tribunal. In either forum, however, the dispute was to be conducted by a plenary suit, and not in a summary fashion. The amendments of 1903, as I understand their scope, have made at least one change in these rules. They have conferred jurisdiction upon the District Court to entertain some of the plenary suits which theretofore could only have been brought in a State court or in the Circuit Court, but the other rules of procedure laid down by the Supreme Court are still to be followed. The District Court, sitting as a court of bankruptcy, may still inquire summarily concerning the ownership of property alleged to belong to the bankrupt, although it be found in the possession or custody of a third person. But, if the court should discover that such person is holding the property under a real claim of title or right of possession and is not merely the alter ego of the bankrupt, it is still the duty of the court to desist from pursuing the summary remedy further, and to remit the contestants to a plenary suit, although the suit, instead of being brought in a State court or a Circuit Court of the United States, may now be brought in the District Court itself, and may there be pursued to final judgment."

In *re Manning*, 10 A. B. R. 497, 123 Fed. 180 (D. C. S. Car.): "The court in bankruptcy has no jurisdiction by summary proceedings to collect money from parties who are indebted to the estate of the bankrupt."

In *re Knickerbocker*, 10 A. B. R. 384, 121 Fed. 1004 (D. C. N. Y.): "On the other hand, if, in the exercise of sound judicial discretion, the referee is satisfied that the asserted adverse holding of the third party is in good faith, and without intent to thwart or obstruct a just and equitable distribution of the bankrupt estate among the creditors, the moving party must be relegated for his remedy to an action, and is not entitled to summary relief from this court. * * * The remedy of the trustee, however, must be sought in a plenary suit brought under the provisions of § 23 (b), as amended (Act Feb. 5, 1903, chap. 487, § 8; 32 Stat. 798), either in this court or the proper State tribunal, at his election."

In *re Cohn*, 3 A. B. R. 421, 98 Fed. 75 (D. C. N. Y.): This case also was decided before the Amendment of 1903 but was placed upon the ground that the proceedings were summary, the court saying:

"She was, therefore, in the position of a third person, not only claiming title, but in possession of the business, as much as its intangible nature was capable of being in possession. If there was any fraud as between her and her mother, so that her title could be avoided in favor of the trustee, that could only be inquired into and adjudged in a plenary suit brought against her by the trustee.

Her rights could not be adjudicated in a summary manner by the referee in the bankruptcy proceeding."

In *re Walsh Bros.*, 21 A. B. R. 14, 163 Fed. 352 (D. C. Iowa): "The application of the trustee is for a summary order requiring Burns Bros. to return to him property alleged to have been transferred and delivered to them by the bankrupts a month before the bankruptcy proceedings were instituted. This property, therefore, has never come into the custody of the court of bankruptcy. Burns Bros. appeared before the referee and made claim to the property, and alleged facts plainly showing their title and right to it. The claim so made and asserted is not a mere colorable one, but is one that arose before the bankruptcy proceedings, and clearly appears from the allegations of the answer to be one that is adverse to the bankrupts, though it may be voidable at the election of the trustee. The application of the trustee is in the nature of an independent action by him against Burns Bros., who are not parties to the bankruptcy proceedings, to avoid the transfer because, as he alleges, it is a voidable preference. Such a suit is not a part of the 'proceedings in bankruptcy,' but is a controversy either at law or in equity between the trustee and a third party, within the meaning of § 23, cls. 'a' and 'b,' of the Bankruptcy Act (Act July 1, 1898, c. 541, 30 Stat. 552 [U. S. Comp. St. 1901, p. 3431]). * * * Has a referee in bankruptcy jurisdiction to determine such a controversy, even with the consent of both parties? If the subject matter of a controversy is not within the jurisdiction of a referee, of course, consent will not confer it, and the court upon a petition for review will acquire none, except to determine the jurisdiction of the referee. * * * The word 'court' may include the referee. Section 1 (7). But this obviously means the referee when acting upon a matter of which is given jurisdiction by the act. The jurisdiction of the referee is prescribed by § 38, as follows: * * * "While much of the authority of the court of bankruptcy is exercised by the referee, and rightly so in proceedings in bankruptcy proper, none of these clauses, nor any other provision of the act, confers upon a referee any authority or power to act except in such proceedings. It is easier to state what are not 'proceedings in bankruptcy' than to definitely name all that are; and it is perhaps not advisable to now attempt to accurately distinguish between such proceedings and 'controversies at law and in equity between trustees as such and adverse claimants concerning the property claimed by the trustees.' It is sufficient for the present to know that it is definitely settled by the Supreme Court in the cases before cited that an action by a trustee to recover property from a third party which is alleged to have been transferred by the bankrupt prior to the bankruptcy as a preference is not a 'proceeding in bankruptcy,' within the meaning of the Bankruptcy Act. If the application of the trustee in question can be upheld as a part of the proceedings in bankruptcy, then a suit to set aside a conveyance of real estate, or an action to recover real property, or any action at law or suit in equity against a third party claiming to own the property as against the bankrupt, might also be brought before the referee, and the only requisite to his jurisdiction would be that the bankrupt once owned the property sought to be recovered. This proposition cannot be assented to. When a referee may, and when he may not, proceed summarily in bankruptcy proceedings before him, is well illustrated in two cases in the Supreme Court, viz, *Mueller v. Nugent*, * * * and *Louisville Trust Co. v. Cominger*. * * * The rule deducible from these decisions is that, where a third party holds property at the time of the bankruptcy merely as agent or bailee of the bankrupt, he may be summarily required by the referee or the court of bankruptcy to turn the property over to the trustee; but where he acquires the possession prior to the bankruptcy, and claims the right to hold the property as against the bankrupt

or the trustee, then the authority of the referee, and of the court of bankruptcy in summary proceedings is limited to determining whether the claim made is colorable merely, or is in fact adverse to the bankrupt, and according as it determines that question will it deny or retain jurisdiction of the controversy. * * * In the present case there can be no doubt that Burns Bros. set forth in their answer facts showing that they acquired possession of the property prior to the bankruptcy, and asserted a claim thereto adverse to the bankrupts, and offered evidence before the referee tending to support such claim. Upon this appearing, the referee should have declined to proceed further with the controversy and permitted the trustee to resort to a court of competent jurisdiction to recover the property, if he, or the creditors, should so elect." Quoted further at § 1796.

In *re Carlile*, 29 A. B. R. 373, 199 Fed. 612 (D. C. N. Car.): "It is a mistake to suppose that all persons having transactions with one who is adjudged a bankrupt, acquiring rights of property adverse to the bankrupt, and therefore to his trustee, who succeeds to the bankrupt's rights, may be drawn, without their consent, into the bankruptcy court before the referee, and such rights summarily dealt with, depriving them of trial by jury and other rights which, but for the intervening bankruptcy, are secured to them. Such a person is not required to go into the bankruptcy court to assert his rights, nor can he, without his consent, be drawn into it by summary process. It is equally clear that if one be in possession of property as the bailee or agent of the bankrupt, or if he takes from the possession of the trustee property belonging to the bankrupt, he may, upon notice, be summarily ordered to surrender such property to the trustee. *Mueller v. Nugent*, 184 U. S. 1, 7 Am. B. R. 224, 22 Sup. Ct. 269, 46 L. Ed. 405. The referee may, upon petition of the trustee, and upon notice to such person, proceed to ascertain whether the person in possession is a bailee or agent, or otherwise holds such possession for the bankrupt, or whether he is an adverse claimant. If, upon such examination, he finds that such person is an adverse claimant, he must dismiss the petition and remit the trustee to his plenary action; otherwise, he may order the delivery of the property to the trustee."

§ 1653. Before Amendment of 1903 Neither Summary nor Plenary Jurisdiction over Adverse Claimants Existed in Bankruptcy Court.—By the decision of the United States Supreme Court in 1900 in the famous case of *Bardes v. Bank*, cited and quoted below, it was established that no jurisdiction, except by consent, existed in the United States Bankruptcy Courts over adverse claimants, and that such suits could only be brought in the State Courts, or in cases of diversity of citizenship, etc., in the United States Circuit [now District] Court.

Coder v. Arts, 213 U. S. 223, 22 A. B. R. 1: "The Bankruptcy Act, as originally passed, did not give the bankruptcy courts jurisdiction over plenary suits to recover the property alleged to belong to the trustee in bankruptcy, except with the consent of the defendant. This was the subject of full consideration and determination in *Bardes v. First Nat. Bank*, 178 U. S. 524. Subsequent decisions of the court construed the act to give the bankruptcy courts jurisdiction over controversies concerning the property in the possession of the bankruptcy courts."

Of course, since no jurisdiction over such claimants existed in the bankruptcy court at all, a fortiori no jurisdiction existed over them by summary

proceedings. Thereupon, in 1903, Congress amended the Act so as to confer upon the bankruptcy courts (the United States District Courts sitting in Bankruptcy) jurisdiction over suits brought by trustees for the recovery of property or the proceeds of property that had been preferentially or fraudulently transferred by the bankrupt within the four months preceding the bankruptcy, or which otherwise had been transferred by transactions that would have been voidable by creditors had there been no bankruptcy. The Amendment, as later will be noted, does not confer jurisdiction over suits of all kinds in which the trustee is interested, but only over those brought by him for the recovery of property or its proceeds where the property has been transferred by voidable transfer. Likewise, as later will be noted, this additional jurisdiction conferred by the amendment was not to be exercised by summary process, but by regular plenary action. Therefore, the summary jurisdiction exercisable by the bankruptcy courts was not enlarged whatever by the Amendment of 1903, but was left precisely as it existed prior to the amendment.

Although, then, the decisions before the Amendment of 1903 as well as those since, deny jurisdiction to the bankruptcy court over adverse claimants by summary process, few of them place the denial squarely upon the single ground that the attempt to exercise it was by summary process, but rather upon the more inclusive ground that no jurisdiction whatever over adverse claimants existed. So the cases before the Amendment of 1903 are not, in general, strictly in point under the proposition that no summary jurisdiction over adverse claimants exists in the bankruptcy courts. Yet, in order to understand the scope of the Amendment, it is proper to consider the law as it stood before the Amendment.²

2. See history as set forth in *In re Andre*, 13 A. B. R. 134, 135 Fed. 736 (C. C. A. N. Y.), quoted ante, at § 1652. *Louisville Trust Co. v. Cominger*, 7 A. B. R. 421, 184 U. S. 18 (affirming *Sinsheimer v. Simonson*, 5 A. B. R. 537, 107 Fed. 898, C. C. A. Ky., discussed in *re Michie*, 8 A. B. R. 737, 116 Fed. 749); *Mitchell v. McClure*, 4 A. B. R. 177, 178 U. S. 539 (affirming 1 A. B. R. 53, 91 Fed. 621); *Burnett v. Morris Mercantile Co.*, 1 A. B. R. 229, 91 Fed. 365 (D. C. Ore.); obiter, *Tesmacher v. Mrazay*, 11 A. B. R. 549, 127 Fed. 728 (D. C. Pa.); *Perkins v. McCauley*, 3 A. B. R. 445 (D. C. Calif., reversed sub nom. *In re San Gabriel Sanatorium*, 4 A. B. R. 197, 102 Fed. 310, C. C. A. Calif.); obiter, *Heath v. Shaffer*, 2 A. B. R. 98, 193 Fed. 647 (D. C. Iowa); compare, *In re Greater Am. Exp.*, 4 A. B. R. 486, 102 Fed. 986 (C. C. A. Neb.); *In re Carter*, 1 A. B. R. 160 (Ref. Ga.); *In re Grahns*, 1 A. B. R. 465 (Ref. Ohio); *In re Michie*, 8 A. B. R. 734, 116 Fed. 749 (D. C. Mass.); *In re Kelly*, 1 A. B. R. 306, 91 Fed. 504 (D. C. Tenn.);

Wall v. Cox, 5 A. B. R. 727, 181 U. S. 244 (101 Fed. 403). Obiter, *In re Walsh Bros.*, 21 A. B. R. 14, 163 Fed. 352 (D. C. Iowa).

Inferentially, *Mueller v. Nugent*, 7 A. B. R. 224, 184 U. S. 1, discussed in *In re Michie*, 8 A. B. R. 736, and quoted under topic of "Summary Orders," post, § 1822. Obiter, *Mueller v. Bruss*, 8 A. B. R. 445, 112 Wis. 406 (Sup. Ct. Wis.). *In re Nixon*, 6 A. B. R. 693, 698, 110 Fed. 633 (D. C. Mont.).

In re Silberhorn, 5 A. B. R. 568, 105 Fed. 809 (D. C. Ills.), although in this case the res was in the custody of the bankruptcy court, and therefore the case was wrongfully decided.

Goodier v. Barnes, 2 A. B. R. 328, 94 Fed. 798 (U. S. C. C. N. Y.).

Apparently, contra, *In re Moody*, 12 A. B. R. 718, 131 Fed. 525 (D. C. Iowa): In this case, however, the facts show the bankrupt had actual custody though an adverse claim existed.

Cases before Amendment of 1903, holding bankruptcy court had jurisdiction to entertain plenary suits by trus-

The Supreme Court, in *Bardes v. Bank*, combated the doctrine that § 2 of the Bankruptcy Act conferred jurisdiction over adverse claimants, and showed that the source of such jurisdiction, if any existed, must be found elsewhere.

Bardes v. Bk., 178 U. S. 524, 4 A. B. R. 163: "In *Lathrop v. Drake*, 91 U. S. 516, the jurisdiction conferred on the District Courts and the Circuit Courts of the United States by the Bankrupt Act of 1867 was defined by this court, speaking by Mr. Justice Bradley, as consisting of 'two distinct classes; first, jurisdiction, as a court of bankruptcy, over the proceedings in bankruptcy, initiated by the petition, and ending in the distribution of assets amongst the creditors, and the discharge or refusal of a discharge of the bankrupt; secondly, jurisdiction, as an ordinary court, of suits at law or in equity, brought by or against the assignee in reference to alleged property of the bankrupt, or to claims alleged to be due from or to him,' and the jurisdiction of the District and Circuit Courts over suits to recover assets of the bankrupt from a stranger to the proceedings in bankruptcy brought by the assignee in a district other than that in which the decree in bankruptcy had been made, was upheld, not under the provisions of § 1 of that act, giving to the District Court original jurisdiction of proceedings in bankruptcy, and of § 2, giving to the Circuit Court supervisory jurisdiction over such proceedings; but wholly under the distinct clause of § 2, which gave to those two courts concurrent jurisdiction of all suits, at law or in equity, brought 'by the assignee in bankruptcy against any person claiming an adverse interest, or by such person against such assignee, touching any property or rights of property of said bankrupt transferable to or vested in such assignee.' * * *

"The jurisdiction of the courts of the United States over all matters and proceedings in bankruptcy, as distinguished from independent suits at law or in equity, was of course exclusive. But it was well settled that the jurisdiction of such suits, conferred by the second section of the Act of 1867 upon the circuit and District Courts, of the United States for the benefit of an assignee in bankruptcy, was concurrent with that of the State courts. * * *

"The section (§ 2) nowhere mentions civil actions at law, or plenary suits in equity. And no intention to vest the courts of bankruptcy with jurisdiction to entertain such actions and suits can reasonably be inferred from the grant of the incidental powers, in clause 6, to bring in and substitute additional parties 'in proceedings in bankruptcy,' and in clause 15, to make orders, issue

tees. Some cases before the Amendment of 1903 maintained erroneously that the bankruptcy courts had jurisdiction to entertain plenary suits by trustees: *Carter v. Hobbs*, 1 A. B. R. 215, 92 Fed. 594 (D. C. Ind.); *In re Kerski*, 2 A. B. R. 79 (Ref. Wis.); *In re San Gabriel Sanatorium*, 4 A. B. R. 197, 102 Fed. 310 (C. C. A. Calif.), reversed *Perkins v. McCauley*, 3 A. B. R. 445 (C. C. A.); *Norcross v. Nathan*, 3 A. B. R. 613 (D. C. Nev.); *Lehman v. Crosby*, 3 A. B. R. 662 (D. C. N. Y.); *Cox v. Wall*, 3 A. B. R. 664, 99 Fed. 546 (D. C. N. Car., affirmed in 4 A. B. R. 659, but reversed by Sup. Ct., 5 A. B. R. 727); *In re Newberry*, 3 A. B. R. 158 (D. C. Mich.); *Murray*

v. Beale, 3 A. B. R. 284 (D. C. Utah); *Louisville Trust Co v. Marx*, 3 A. B. R. 450 (D. C. Ky.); *Pepperdine v. Headley*, 3 A. B. R. 455 (D. C. Mo.); *In re Woodbury*, 3 A. B. R. 457 (D. C. N. Dak.); *Shutts v. Bank*, 3 A. B. R. 492, 98 Fed. 705 (D. C. Ind.). Obiter, *In re Hammond*, 3 A. B. R. 466, 98 Fed. 845 (D. C. Mass.): But this case is wholly obiter on this point, for it was a case of a lien by legal proceedings nullified by bankruptcy as to which the bankruptcy court always has had summary jurisdiction. Obiter, *Robinson v. White*, 3 A. B. R. 88 (D. C. Ind.). Obiter, *In re Sievers*, 1 A. B. R. 117, 91 Fed. 366 (D. C. Ky.).

process and enter judgments, 'necessary for the enforcement of the provisions of this act.'

"The chief reliance of the appellant is upon clause 7. But this clause, in so far as it speaks of the collection, conversion into money and distribution of the bankrupt's estate, is no broader than the corresponding provisions of section 1 of the Act of 1867; and in that respect, as well as in respect to the further provision authorizing the court of bankruptcy to 'determine controversies in relation thereto, it is controlled and limited by the concluding words of the clause, 'except as herein otherwise provided.'

"These words, 'herein otherwise provided,' evidently refer to § 23 of the act, the general scope and object of which, as indicated by its title, are to define the jurisdiction of United States and State Courts in the premises. The first and second clauses are the only ones relating to civil actions and suits at law or in equity.

"The first clause provides that 'the United States Circuit Courts shall have jurisdiction of all controversies at law and in equity, as distinguished from proceedings in bankruptcy' (thus clearly recognizing the essential difference between proceedings in bankruptcy, on the one hand, and suits at law or in equity, on the other), 'between trustees as such and adverse claimants, concerning the property acquired or claimed by the trustees,' restricting that jurisdiction, however, by the further words, 'in the same manner and to the same extent only as though bankruptcy proceedings had not been instituted and such controversies had been between the bankrupts and such adverse claimants.' This clause, while relating to the Circuit Courts only, and not to the District Courts of the United States, indicates the intention of Congress that the ascertainment, as between the trustee in bankruptcy and a stranger to the bankruptcy proceedings, of the question whether certain property claimed by the trustee does or does not form part of the estate to be administered in bankruptcy, shall not be brought within the jurisdiction of the national courts solely because the rights of the bankrupt and of his creditors have been transferred to the trustee in bankruptcy.

"The second clause positively directs that 'suits by the trustee shall only be brought or prosecuted in the courts where the bankrupt whose estate is being administered by such trustee might have brought or prosecuted them if proceedings in bankruptcy had not been instituted, unless by consent of the proposed defendant.'

"But the second clause applies both to the District Courts and to the Circuit Courts of the United States, as well as to the State courts. This appears, not only by the clear words of the title of the section, but also by the use of this clause of the general words, 'the courts,' as contrasted with the specific words, 'the United States Circuit Courts,' in the first and in the third clauses.

"Had there been no bankruptcy proceedings, the bankrupt might have brought suit in any State court of competent jurisdiction; or, if there was a sufficient jurisdictional amount, and the requisite diversity of citizenship existed, or the case arose under the Constitution, laws or treaties of the United States, he could have brought suit in the Circuit Court of the United States. Act of August 13, 1888, c. 866, 25 Stat. 434. He could not have sued in a District Court of the United States, because such a court has no jurisdiction of suits at law or in equity between private parties, except where, by special provision of an act of Congress, a District Court has the powers of a Circuit Court, or is given jurisdiction of a particular class of civil suits.

"It was argued for the appellant that the clause cannot apply to a case like the present one, because the bankrupt could not have brought a suit to set aside a conveyance made by himself in fraud of his creditors. But the clause

concerns the jurisdiction only, and not the merits, of a case; the forum in which a case may be tried, and not the way in which it must be decided; the right to decide the case, and not the principles which must govern the decision. The bankrupt himself could have brought a suit to recover property, which he claimed as his own, against one asserting an adverse title in it; and the incapacity of the bankrupt to set aside his own fraudulent conveyance is a matter affecting the merits of such an action, and not the jurisdiction of the Court to entertain and determine it.

"The Bankrupt Acts of 1867 and 1841, as has been seen, each contained a provision conferring in the clearest terms on the Circuit and District Courts of the United States concurrent jurisdiction of suits at law or in equity between the assignee in bankruptcy and an adverse claimant of property of the bankrupt. We find it impossible to infer that when Congress, in framing the Act of 1898, entirely omitted any similar provision, and substituted the restricted provisions of § 23, it intended that either of those courts should retain the jurisdiction which it had under the obsolete provision of the earlier acts.

"On the contrary, Congress, by the second clause of § 23 of the present Bankrupt Act, appears to this court to have clearly manifested its intention that controversies, not strictly or properly part of the proceedings in bankruptcy, but independent suits brought by the trustee in bankruptcy to assert a title to money or property as assets of the bankrupt against strangers to those proceedings, should not come within the jurisdiction of the District Courts of the United States, 'unless by consent of the proposed defendant,' of which there is no pretense in this case."

Jacquith v. Rowley, 188 U. S. 620, 9 A. B. R. 528: "The objection that it is not a suit within the meaning of the 23d section of the Bankruptcy Law is without force. The proceeding was a summary application to the court in bankruptcy to grant an order in a matter, the result of the granting of which would be to immediately take from the surety moneys which had been deposited with him before the commencement of the proceedings in bankruptcy, and thus compel him to come into the bankruptcy court for the litigation of questions as to his right to retain the money claimed by him. It would also enjoin the plaintiffs in the State suits from proceeding to collect their judgments from the surety in the bail bonds. To extend such a jurisdiction over an adverse claimant would be within the prohibition of § 23, a and b * * * whether such jurisdiction were exerted by an action strictly so-called or by a summary application to the court in bankruptcy. It is the exercise of jurisdiction which the section prohibits, and the particular method of procedure in the court is immaterial. The surety in whose hands the money was deposited to indemnify him for his liability on the bail bond was an adverse claimant within the meaning of that section of the act, and could not be proceeded against in the bankruptcy court unless by his consent, as provided for therein."

Bank v. Title & Trust Co., 198 U. S. 280, 14 A. B. R. 106 (reversing *In re Rodgers*, 11 A. B. R. 78, 125 Fed. 569): "The distinction between steps in bankruptcy proceedings proper and controversies arising out of the settlement of the estates of bankrupts is recognized in §§ 23, 24 and 25 of the present Act. * * * This distinction existed under the prior bankruptcy law, and the then decisions in respect of a proceeding in bankruptcy and an independent suit are applicable. It was settled that the bankruptcy court was without jurisdiction to determine adverse claims to property, not in the possession of the assignee in bankruptcy, by summary proceedings, whether absolute title or only a lien was asserted. * * *

"The present Act was plainly framed in recognition of the principle of these cases."

In *re Baudouine*, 3 A. B. R. 651, 101 Fed. 574 (C. C. A. N. Y.): “* * * the language of clause 7 (of § 2) would seem to be sufficiently comprehensive to authorize the determination by Courts of Bankruptcy of every controversy relating to the estates of bankrupts. * * * Nevertheless, it is capable of a narrower construction, and can be read as extending only to controversies about property which actually belongs to the bankrupt’s estate, or which arise strictly in the bankruptcy proceeding, such as those in reference to the marshaling of assets, or the extent and priority of conflicting liens.”

Obiter, In *re Rochford*, 10 A. B. R. 608, 124 Fed. 182 (C. C. A. S. Dak.): “The District Court sitting in bankruptcy has no jurisdiction over a controversy between trustees in bankruptcy and an adverse claimant relating to the title or possession of property in the custody of the latter, in the absence of his consent, but such an issue is a controversy at law or in equity, as distinguished from a proceeding in bankruptcy, within the meaning of § 23 of the Bankrupt Act of 1898.”

Sheldon v. Parker, 11 A. B. R. 170, 92 N. W. 923, 66 Neb. 610: “Under the law his official character as trustee gives him no greater right to commence an action in the Federal court against residents of this State than he possessed as an individual, and the Federal Congress, having relegated such cases to the jurisdiction of the State courts, has conferred upon the State court full authority to act, and to tax the usual costs and expenses attending such suits, the same as in other cases.”

In *re Sheinbaum*, 5 A. B. R. 187, 107 Fed. 247 (D. C. N. Y.): “The evidence shows that Wasserman was in possession claiming title before the bankruptcy, and hence, under *Bank v. Bardes*, I cannot oust him by summary proceedings, except he consent to proceedings in this court.”

In *re Ward*, 5 A. B. R. 217, 104 Fed. 985 (D. C. Mass.): “* * * the district court is without jurisdiction to take property alleged to belong to the bankrupt out of the possession of a third party, as well temporarily and by summary process, as permanently and by plenary suit.”

Hicks v. Knost, 2 A. B. R. 153, 94 Fed. 625 (D. C. Ohio): “Now, is it necessary, within the meaning of the law, in order to accomplish these ends, to invest bankruptcy courts with jurisdiction to hear and determine all controversies incident to the collection and conversion into money of the bankrupt’s estate? Must all suits and actions for that purpose, actions on accounts, promissory notes and contracts, and suits to foreclose mortgages, set aside fraudulent conveyances and the like, be brought in the bankruptcy courts without reference to the amount involved, the citizenship of the parties, or the questions presented. Must the dockets be crowded and the time of the District Courts be taken up with the hearing of minor controversies at great inconvenience and expense to the litigants, who may be compelled to travel long distances to attend the courts, or was it the intention of Congress to follow its long-established policy of permitting such controversies to be determined in the local State courts, at the doors of the people without necessary expense or inconvenience? * * *

“It seems to me that it was the intention of Congress to permit such controversies, when they could not be settled by compromise or arbitration, to be litigated in the courts, which, under the general law, would have jurisdiction of them, just as assignees under State insolvency laws bring suits in courts of general jurisdiction to collect assets which are afterwards distributed by the Court of Insolvency. The Bankruptcy Court controls the trustee, supervises the administration of his trust, settles his accounts and orders the distribution of the moneys in his hands, but is not required to assume the burden of the litigations necessary for the collection of assets, nor are adverse claimants of

property, acquired or claimed by trustees, to be put to unnecessary inconvenience and expense in litigating their rights."

In *re Steuer*, 5 A. B. R. 213, 104 Fed. 976 (D. C. Mass.): "*Bardes v. Bank* must be taken to decide that a trustee cannot, by petition in bankruptcy, recover from a third party property alleged to belong to the bankrupt's estate, if objection is seasonably taken to the form of the proceedings. Even with the defendants' consent to the general jurisdiction of the court, the court must, if the defendant insists, proceed by plenary suit. But *Stickney v. Wilt*, *Milner v. Meek*, and perhaps *White v. Ewing* must still be taken to authorize a proceeding by way of petition where (1) the court has jurisdiction to proceed by way of plenary suit, (2) where no seasonable objection is taken to the form of procedure, and (3) where, under the forum of a petition in bankruptcy, the rights of the respondent are secured as substantial as in a plenary suit. In the case at bar no objection was made to the form of proceeding until the argument before the District Court, and, inasmuch as this court has, through the defendants' submission thereto, jurisdiction by way of plenary suit of the proceedings in question, the objection to the form of proceedings has come too late."

§ 1654. Injunctions on Adverse Claimants Issuable in Bankruptcy Proceedings.—The doctrine of *Bardes v. Bank* does not affect the jurisdiction of the Bankruptcy Court to issue restraining orders and injunctions in the bankruptcy proceedings themselves, upon adverse claimants in possession, in aid of the bankruptcy proceedings to preserve the status quo: it affects merely the forum for the recovery of property and debts.³ However some courts have held that injunctions come under the same doctrine; that the enjoining of the disposition of property is the exercise of the same right involved in the ordering of its surrender.⁴

But restraining a litigant in the State court from proceeding further therein is to be distinguished from restraining the court or its officers.⁵

§ 1654½. Whether "Adverse Claimant in Possession" Determined by Pleadings.—The bankruptcy court has jurisdiction in the summary proceedings to determine the existence of the facts requisite to give it the jurisdiction to proceed summarily.⁶

Nevertheless, it will only examine far enough to determine whether the facts are alleged in good faith (even though they be fraudulent) and whether, if true, they would constitute the adverse party an "adverse claimant" within the meaning of the law.⁷

And it has been held that the bankruptcy court is not concluded by the

3. In *re Currier*, 5 A. B. R. 629 (Ref. N. Y.); In *re Tiffany*, 13 A. B. R. 310, 133 Fed. 799 (D. C. N. Y.). Also, see post, "Restraining Orders and Injunctions in Aid of Bankruptcy Proceedings," § 1901, et seq. Compare, impliedly, In *re Donnelly*, 26 A. B. R. 304, 188 Fed. 1001 (D. C. Ohio). Inferentially, In *re Norris*, 24 A. B. R. 444, 177 Fed. 598 (D. C. N. Y.); *Pyle v.*

Texas, etc., Co., 25 A. B. R. 829, 185 Fed. 309 (D. C. La.).

4. In *re Ward*, 5 A. B. R. 215, 104 Fed. 985 (D. C. Mass.). Instance, In *re George A. Glenn*, 25 A. B. R. 806, 185 Fed. 554 (D. C. Pa.).

5. In *re Roger Brown & Co.*, 28 A. B. R. 336 (C. C. A.).

6. See post, § 1863.

7. See post, § 1864.

pleadings but may inquire into the facts to see if the claim is really adverse or merely colorably so; but if really adverse, although fraudulent and voidable or not sustainable by the weight of the evidence, summary jurisdiction will not be assumed.⁸

DIVISION 1.

WHO ARE ADVERSE CLAIMANTS.

§ 1655. "Adverse Claimants" Not Confined to Absolute Owners.—"Adverse claimant" is a term not to be confined to those who claim absolute ownership.⁹ Thus a surety holding funds of his principal as indemnity, placed there coincidentally with the signing of the bail bonds, may not be proceeded against summarily.¹⁰ Chattel mortgagees and vendees of bills of sale, are adverse claimants where the trustee claims they are fraudulent.¹¹

One who has a substantial claim to a mortgage lien antedating the bankruptcy is equally an adverse claimant with one who claims absolute title.¹²

Of course, one who denies the possession, and makes no claim of title to property which is alleged to be in his possession, cannot consistently object to summary proceedings for the recovery of such property, on the ground that he is an "adverse claimant."¹³

§ 1656. Adverse Claimant and Bankrupt Holding Jointly, Bankruptcy Court Has Jurisdiction.—But where such third person has not the exclusive possession, but holds along with the bankrupt, the bankruptcy court may have jurisdiction.¹⁴

§ 1657. Adverse Claimant Obtaining Voluntary Possession from Bankruptcy Officer Whether Subject to Summary Jurisdiction.—It has been held that one gaining possession voluntarily from the receiver in bankruptcy, if he be an "adverse claimant," may not be proceeded against summarily by the trustee to regain possession, the summary jurisdiction previously existing being extinguished by the gaining of such voluntary possession.

8. See, § 1865.

9. *Jacquith v. Rowley*, 9 A. B. R. 528, 188 U. S. 620; *Bank v. Title Trust Co.*, 14 A. B. R. 106, 198 U. S. 280 (reversing *In re Rodgers*, 11 A. B. R. 78, 125 Fed. 569); (1867) *Smith v. Mason*, 14 Wall. 419; (1867) *Marshall v. Knox*, 16 Wall. 551; (1867) *In re Bonesteel*, 7 Blatchf. 175; (1867) *Knight v. Cheney*, 14 Fed. Cas. 60; (1867) *In re Ballou*, 4 Ben. 135; (1867) *In re Marter*, 16 Fed. Cas. 857; instance, *In re Mimms and Parham*, 27 A. B. R. 469, 193 Fed. 276 (D. C. Ky.).

10. *Jacquith v. Rowley*, 9 A. B. R. 528, 188 U. S. 620; *In re Horgan*, 19 A. B. R. 857, 158 Fed. 774 (C. C. A. Mont.); *In re Horgan*, 21 A. B. R. 31, 164 Fed. 415 (C. C. A. Mont.).

11. *Small v. Mueller*, 8 A. B. R. 448, 67 App. Div. 143.

Government, as to Rewards for Information Given by Bankrupt in Aid of Detection of Smugglers.—*Obiter*, *In re Ghazal*, 20 A. B. R. 807, 163 Fed. 602 (D. C. N. Y.).

12. *In re Rathman*, 25 A. B. R. 246, 183 Fed. 913 (C. C. A. S. D.).

13. *In re Fogelman*, 26 A. B. R. 742, 188 Fed. 755 (D. C. N. Y.).

14. *In re Brooks*, 1 A. B. R. 531, 91 Fed. 508 (D. C. Vt.).

But compare cases, where, however, the facts are so meagre on the point of who had actual possession or control of the real estate as to baffle analysis. *In re Pickens & Bro.*, 26 A. B. R. 6, 184 Fed. 954 (D. C. Ga.).

sion afterwards.¹⁵ This is doubtless true where it is the trustee from whom the possession was obtained; but, on the other hand the opposite has been held where it is the receiver from whom the possession was obtained, since the receiver has no power to make a voluntary surrender.¹⁶

Thus, a holder of a receiver's certificate has been held subject to summary order to return money paid on the certificate by the receiver contrary to the court's order.¹⁷

§ 1657½. Creditors Receiving Property after Filing of Petition, Not "Adverse" When.—Creditors receiving property from the bankrupt, which was once in the custody of the receiver in bankruptcy but had been released by him to the bankrupt under order of court (because of the receiver's failure to qualify), have been held not to be adverse claimants, but to be subject to summary jurisdiction.^{17a}

§ 1658. Adverse Claimant Himself Becoming Bankrupt Gives Jurisdiction.—Adverse claimant becoming bankrupt gives jurisdiction to the bankruptcy court as between the two trustees in bankruptcy.¹⁸

§ 1659. Attaching Creditor Receiving Proceeds, within Four Months, Adverse Claimant.—An execution or attaching creditor in receipt of the proceeds of the execution or attachment sale before the bankruptcy although within the four months, is an adverse claimant,¹⁹ but is not such adverse claimant when he receives the property itself by virtue of a redelivery bond.²⁰

§ 1660. Receiving Proceeds after Bankruptcy, Not "Adverse Claimant."—But where the attaching or execution creditor receives the proceeds afterward and with knowledge of the filing of the petition, the creditor is not an adverse claimant; for this would be a case where it was not in the possession of the creditor at the "time of bankruptcy."²¹ However, the rule would be different if the property were exempt and claimed as such, even though, after the proceeds were paid over, the bankrupt attempted to waive the exemption.^{21a}

§ 1661. Proceeds Still in Officer's Hands; Neither Creditor nor Officer Adverse Claimant.—Nor are such creditors adverse parties where

15. *Hinds v. Moore*, 14 A. B. R. 1, 134 Fed. 221 (C. C. A. Tenn., reversing *In re Leeds Woolen Mills*, 12 A. B. R. 136, 129 Fed. 922).

16. See post, § 1801; *Whitney v. Wenman*, 14 A. B. R. 45, 198 U. S. 539, 552; *In re Burkhalter & Co.* (*Rogers v. People's Bank*), 24 A. B. R. 553, 179 Fed. 403 (D. C. Ala.); *obiter*, *In re Rose Shoe Mfg. Co.*, 21 A. B. R. 725, 168 Fed. 39 (C. C. A. N. Y.).

17. *In re Burkhalter & Co.* (*Rogers v. People's Bank*), 24 A. B. R. 553, 179 Fed. 403 (D. C. Ala.).

17a. See post, § 1800. Also, see *Knapp & Spencer v. Drew*, 20 A. B. R. 355, 160 Fed. 413 (C. C. A. Neb.).

18. *In re Rosenberg*, 8 A. B. R. 624, 116 Fed. 402 (D. C. Penn.).

19. See ante, §§ 1477 and 1478.

20. *In re Cohn*, 18 A. B. R. 786 (Ref. Calif.). Also, see §§ 1661, 1662.

21. See ante, § 1484, and post § 1800.

21a. *In re Edwards*, 19 A. B. R. 632, 156 Fed. 794 (D. C. Ala.).

the proceeds are still in the hands of the court or officer at the time of the adjudication of bankruptcy;²² nor is the officer an adverse claimant.²³

§ 1662. Court Officers in Possession, Adverse Claimants until Adjudication.—Court officers in possession of property are not subject to the summary jurisdiction of the bankruptcy court until adjudication has nullified the liens. Thus, a sheriff holding the proceeds of an attachment sale in his hands after the filing of the bankruptcy petition but before adjudication, is an adverse claimant where he is claiming a lien thereon for poundage. He represents a creditor and is holding adversely to the bankrupt by a lien that is not yet void.²⁴ And they are not adverse claimants after adjudication,²⁵ and may be summarily ordered to surrender the property in their possession.²⁶

But it has been held, though on doubtful authority, that court officers in possession, where the property itself is not under the direct custody of the court as it would be in cases of judicial sales and is being simply held for execution sale, may be ordered to turn over the property, notwithstanding the execution levy and lien were obtained before the four months' period and are therefore good, the lien following the property into the trustee's hands for administration.²⁷

§ 1663. Whether Garnishee Adverse Claimant Where Garnishment within Four Months.—The courts have appeared, in some decisions, to incline somewhat to the doctrine that the garnishee is not an adverse claimant, where the garnishment is instituted within the four months preceding the bankruptcy.²⁸

The true rule would seem to be that the garnishee is an adverse claimant if he claims any interest in or lien upon the property in his possession, or if he is a mere debtor of the bankrupt; and that if he is a debtor of the bankrupt or is in possession of property under claim of a right thereto or an interest therein, he is not subject to summary process; the fact that he is a garnishee not changing the usual rules in these respects.

In *re Kane*, 18 A. B. R. 654, 152 Fed. 587 (D. C. Pa.): "I do not think the referee gave sufficient weight to the attachment proceedings in the com-

²². See ante, §§ 1477, 1478 and 1479. Also, see *In re Grassler & Reichwald*, 18 A. B. R. 694, 154 Fed. 478 (C. C. A. Calif.).

²³. In *re Cohn*, 18 A. B. R. 786 (Ref. Calif.).

Obiter [surrender not required, but on other grounds], also impliedly [not proceeds but property itself pursued], *Staunton v. Wooden*, 24 A. B. R. 736, 179 Fed. 61 (C. C. A. Calif.).

²⁴. In *re Andre*, 13 A. B. R. 132, 135 Fed. 736 (C. C. A. N. Y.); post, § 1818 and § 1828.

²⁵. In *re Cohn*, 18 A. B. R. 786 (Ref. Calif.); *Obiter*, *Staunton v. Wooden*,

24 A. B. R. 736, 179 Fed. 61 (C. C. A. Cal.).

²⁶. See ante, § 1474.

²⁷. In *re Vastbinder*, 13 A. B. R. 148 (D. C. Penn.); In *re Booth*, 2 A. B. R. 770, 96 Fed. 943 (D. C. Ga.). See §§ 1488½, 1807.

²⁸. *Quære*, *obiter*, In *re Beals*, 8 A. B. R. 639, 116 Fed. 530 (D. C. Ind.); compare, In *re Sharp*, 1 A. B. R. 379 (Ref. Ky.). Compare, In *re McCartney*, 6 A. B. R. 367 (D. C. Wis.), which was a case where the garnishee itself prayed leave to pay over exempt wages to the bankruptcy court and its petition was granted.

mon pleas of Philadelphia county. These were begun nearly three months before the petition in bankruptcy was filed, and J. Joseph Murphy was summoned as garnishee. He then held in his hands, and still holds, the sum of \$500, to which, either in whole or in part, there are several claimants, including each of the bankrupts. The money has never been in the control of the District Court, and its ownership is a fairly disputable question. Clearly, as it seems to me, the Court of Common Pleas is the proper tribunal to settle this controversy, unless all parties in interest have submitted themselves to the court in bankruptcy. The referee thought that such submission had been made, and therefore decided the case on the merits, and entered an order directing the garnishee to pay over to Mary Murphy the \$500 now in his hands. In making this order, I think the referee was in error. It may be that Mary Murphy, Kane and Sweeney did submit themselves to the jurisdiction of the District Court, but it is plain that the garnishee declined to follow this course, and that he has an individual claim upon part of the fund."

The cases affirming summary orders on garnishees have been either cases where the point was not raised or where there was no adverse claim on the part of the garnishee and where the garnishee was simply a stakeholder.

§ 1664. Wife "Adverse Claimant" as to Property She May Hold Adversely to Husband.—The bankrupt's wife may be an adverse claimant in Alabama;³⁰ also in Pennsylvania;³¹ also in New York.³²

Money saved by the wife from allowances made to her for household expenses may, under some circumstances, be retained by her as against the trustee in bankruptcy of a partnership of which her husband was a member.

In re Simon No. 2, 28 A. B. R. 616, 197 Fed. 102 (D. C. N. Y.): "It has been broadly held, as contended by counsel for the trustees, that money saved by a wife from an allowance by her husband for household expenses belongs to him; yet such adjudications proceed upon the theory that the wife is the agent for her husband in the conduct of the household affairs, and that, in the absence of an intention to bestow a gift upon her, a trust relationship is created. But this principle is not applicable to the facts under consideration, as the surrounding circumstances, together with the testimony, negative any trust relationship, and clearly support the implication that any amount saved from the weekly allowance was to be the separate property of the wife. The burden of proof rested upon the trustees to show that the presumptions were to the contrary, and that instead of a gift to the wife a trust relationship was created. In this they have failed. The rationale of the entire transaction, the station in life of the parties, the solvency of the donor during the entire period, the economy of the wife in performing her household duties and dispensing with the assistance of servants, all point with persuasive cogency to an intention by the husband to relinquish possession, control, and ownership of the various amounts paid the wife and to vest her with title to unexpended amounts. Knowledge that the wife was in the habit of concealing unused sums was not essential to the validity of the gift. In the cases cited by the counsel for the trustees, of which *Aaronson v. McCauley*, 19 N. Y. Supp. 690, is most directly in point, the holding of the court, that the surplus arising out of the

30. *Blumberg v. Bryan*, 6 A. B. R. 20, 107 Fed. 673 (C. C. A. Ala.).

31. In re *Green*, 6 A. B. R. 270 (D. C. Penn.).

32. Compare (inferentially), In re *Norris*, 24 A. B. R. 444, 177 Fed. 598 (D. C. N. Y.).

economy of the wife in managing her household remains the property of the husband, doubtless rested upon facts showing that there was no intention to bestow the remainder as a gift upon the wife."

Indeed, the bankruptcy court, in the exercise of its equitable jurisdiction, will aid the wife in recovering her separate estate from her husband's trustee in bankruptcy.³³

§ 1665. Assignee or Receiver Not "Adverse Claimant" as to Proceeds Still in Hands.—An assignee or receiver for creditors is not an "adverse claimant," but is an agent of the assignor.³⁴

Bryan v. Bernheimer, 181 U. S. 188, 5 A. B. R. 623: "The general assignment, made by Abraham to Davidson, did not constitute Davidson an assignee for value, but simply made him an agent of Abraham for the distribution of the proceeds of the property among Abraham's creditors."

Similarly, a bank holding a fund produced from the sale of the debtor's entire stock of merchandise made within the four months period under a receipt expressing on its face that the fund was to be pro-rated among the debtor's creditors as their interests might appear, is a mere agent of the bankrupt and may be summarily ordered by the bankruptcy court to surrender the property; and it does not become an adverse holder by virtue of the fact that after the adjudication, without consent of the debtor nor purchaser, it credits the fund on a claim of its own and also on that of one of the other creditors: as the fund was deposited for a special purpose the bank held it as a trustee before the adjudication, and not as an adverse claimant.³⁵ Thus, also, an assignee for creditors under a void general assignment who claims in his individual capacity part of the assets in his possession as assignee, is not in possession as adverse claimant but as assignee.³⁶ The purchaser at a collusive sale by an assignee under a void general assignment preceding the bankruptcy of the assignor is an adverse claimant.³⁷

In *re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio): "The assignee contends in this court that the referee in bankruptcy had no jurisdiction by summary proceeding to direct an assignee appointed under the State law to turn over to the trustee in bankruptcy the funds to which he claims the right to credit, on account of commissions, compensation for extra services, and bills for legal services and expenses. This contention rests upon the proposition that the claim of the assignee is adverse to the estate of the bankrupt. There is no doubt that if the claim presented by the assignee is an adverse claim within the meaning of the decisions, the District Court had no jurisdiction

33. In *re Hoffman*, 28 A. B. R. 680, 199 Fed. 448 (D. C. N. J.).

34. *Whittlesey v. Becker & Co.*, 25 A. B. R. 672 (Sup. Ct. N. Y.); In *re Carver & Co.*, 7 A. B. R. 539, 113 Fed. 128 (D. C. N. Car.).

To same effect even where the assignor is not the bankrupt, but is a mere partner in the bankrupt partner-

ship, see In *re Stokes*, 6 A. B. R. 262, 106 Fed. 312 (D. C. Penn.).

35. In *re Davis*, 9 A. B. R. 670 (D. C. Tex.).

36. In *re Thompson*, 11 A. B. R. 719, 128 Fed. 575 (C. C. A. N. Y.).

37. In *re Findlay Bros.*, 4 A. B. R. 745, 104 Fed. 675 (D. C. N. Y.).

by summary proceeding to require the turning over of the moneys to the estate of the bankrupt as against the assignee's objection to the jurisdiction of the bankruptcy court. *Louisville Trust Co. v. Comingor*, 184 U. S. 18, 7 Am. B. R. 421; *First Nat. Bank v. Title & Trust Co.*, 198 U. S. 280, 14 Am. B. R. 102. But in our opinion, upon the case presented on this review, the District Court had jurisdiction to make the order complained of. The assignment by Hays to Stewart did not constitute the latter an assignee for value, but simply made him the agent of Hays for the distribution of the proceeds of the property among the latter's creditors. Being such agent his possession was that of the principal, and he therefore did not hold adversely to the bankrupt or to the latter's trustee by the mere fact that he held in his hands funds received by him under the assignment. *Bryan v. Bernheimer*, 181 U. S. 188, 192, 193, 5 Am. B. R. 623; *Mueller v. Nugent*, 184 U. S. 1, 17, 7 Am. B. R. 224."

"The assignee contends that this case is ruled by *Louisville Trust Co. v. Comingor*, supra, in which, under the facts there presented, the bankruptcy court was held to have no jurisdiction to make an order for the surrender by an assignee of moneys which had been received by him under the assignment. The *Comingor* case differs from the case before us in these respects: In that case the assignee denied the jurisdiction of the bankruptcy court, and showed in defense to the proceeding to require him to pay over the moneys in question that previous to the commencement of the bankruptcy proceedings he had actually disbursed the entire amount by way of commissions retained by him as compensation and through payments to his attorneys, and that he was utterly unable to recover or repay any part of such moneys. He therefore could not comply with an order for surrender, and as pointed out by this court in the opinion of Judge Severens, imprisonment must inevitably follow the order for surrender. *Ex parte Comingor* (C. C. A., 6th Cir.), 5 Am. B. R. 537, 107 Fed. 898, 907, 47 C. C. A. 51. As stated by Mr. Chief Justice Fuller: 'He (*Comingor*) was ruled to show cause, and the cause he showed defeated jurisdiction over the subject-matter, that is, jurisdiction to proceed summarily. He did not come in voluntarily, but in obedience to peremptory orders, and although he participated in the proceedings before the referee, he had pleaded his claim in the outset, and he made his formal protest to the exercise of jurisdiction before the final order was entered.'

"In the case we are considering, of the \$18,000 and upwards received by the assignee there came into his hands previous to the proceedings in bankruptcy but \$808.12. The accounts presented by him show that he had disbursed previous to the bankruptcy proceedings but \$166. We find no assertion in the record that he has ever paid the claims of Stewart & Stewart for legal services (except the sum of \$99.72, not in controversy) or any of the claims in controversy here except the expenses (as distinguished from legal services) connected with the resistance to the bankruptcy proceedings. The record is express that upon the proceedings for the settlement of his accounts before the referee, the assignee stated in open court, that the entire receipts, less certain disbursements which were allowed by the referee, "should be treated as cash now in the hands of the assignee." The order of the referee is for the surrender to the trustee by the assignee of the "sum of four thousand eighty-six and sixty-one one-hundredths dollars (4,086.61) so as aforesaid in his possession and belonging to said estate."

§ 1666. But "Adverse Claimant" as to Proceeds Already Disbursed.—But an assignee for creditors, as to disbursements made out of the assigned property before the bankruptcy of the assignor, is an adverse

claimant and may not be summarily ordered to account to the bankruptcy court therefor.³⁸ Likewise, an assignee for creditors retaining and expending, before the bankruptcy of the assignor, his commissions out of the assigned property, is an adverse claimant, and may not be summarily ordered to account to the bankruptcy court therefor.³⁹ But an attorney for an assignee, holding property of the estate, is not an adverse claimant, but is subject to summary order.⁴⁰

§ 1667. Agent in Possession Applying Funds on Salary.—Similarly, an agent in possession claiming to have applied, by agreement with the bankrupt, funds in his possession as manager upon his salary, is an adverse claimant; and, as to funds so applied, can only be reached by plenary action, although as to funds not so applied he is subject to summary jurisdiction.⁴¹

§ 1668. Trustee in Possession under Mortgage for Benefit of Certain Creditors, "Adverse Claimant."—A trustee in possession under a mortgage or trust deed made for the benefit of certain creditors, is an adverse claimant, and not subject to summary jurisdiction.⁴²

§ 1669. Alleged but Not Real Partners in Involuntary Partnership Petition, Whether "Adverse Claimants," Subject to Summary Seizures of Property.—Persons alleged to be members of a partnership against whom an involuntary partnership petition is filed, but who are not partners, are adverse claimants, and their property may not be summarily seized.⁴³

§ 1670. Executor Holding Legacy to Bankrupt, Not "Adverse Claimant."—An executor holding a legacy belonging to the bankrupt, is not an adverse claimant.⁴⁴

§ 1671. But Administrator of Deceased Partner in Possession of Firm Assets, "Adverse Claimant."—But the administrator of a deceased partner in possession of firm assets, is an adverse claimant where the other partner is the bankrupt.⁴⁵

38. *Louisville Trust Co. v. Comingor*, 7 A. B. R. 421, 184 U. S. 18 (affirming *Sinsheimer v. Simonson*, 5 A. B. R. 537, 107 Fed. 898); *In re Manning*, 10 A. B. R. 497, 123 Fed. 180 (D. C. S. Car.). Impliedly and on the facts, *In re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio), quoted at § 1665.

39. *Louisville Trust Co. v. Comingor*, 7 A. B. R. 421, 184 U. S. 18 (affirming *Sinsheimer v. Simonson*, 5 A. B. R. 537, 107 Fed. 898); impliedly and on the facts, *In re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio), quoted ante, § 1665.

40. *Obiter*, *In re Michie*, 8 A. B. R. 734, 738, 116 Fed. 749 (D. C. Mass.).

41. *In re Lebrecht*, 14 A. B. R. 445, 135 Fed. 878 (D. C. Tex.).

Whether the party was actually in possession claiming ownership is a question of fact, and the finding of the special master will not be disturbed where there is a conflict of evidence, *In re Kolin*, 13 A. B. R. 533, 134 Fed. 557 (C. C. A. Ills.).

42. *Publishing Co. v. Hutchinson, Co.*, 17 A. B. R. 425 (Sup. Ct. Mich.).

43. *In re Nixon*, 6 A. B. R. 693 (D. C. Mont.).

44. *In re May*, 5 A. B. R. 1 (Ref. Minn., affirmed by D. C.).

45. *In re Pierce*, 4 A. B. R. 489, 102 Fed. 977 (D. C. Wash.).

§ 1672. **Trustees of Spendthrift Trusts, "Adverse Claimants."**—Trustees of spendthrift trusts are adverse claimants.

In *re Baudouine*, 3 A. B. R. 651, 101 Fed. 574 (C. C. A. N. Y., reversing 3 A. B. R. 55, 96 Fed. 536): "He is entitled to insist that he shall not be prevented from paying it to the beneficiary and compelled to pay it to another. If the fund can be reached by the trustee in bankruptcy after it has come into the hands of the bankrupt, the testamentary trustees are not necessary parties to an action. But if it is sought to be reached before they have discharged their fiduciary and statutory obligation towards the beneficiary, they are in duty bound to resist. In defending their trust duties they are hostile to the trustee in bankruptcy, and if they are entitled to be heard at all they are entitled to contest his title as fully as though they were the equitable owners of the fund."

§ 1673. **Mere Bailee in Possession, Not "Adverse Claimant."**—It has been held that a bailee in possession is not an adverse claimant;⁴⁶ even where he has a lien for unpaid services or other charges incident to the bailment.⁴⁷

But this rule must be taken with qualification. If there is no dispute over the amount or validity of his lien and if such amount is tendered him, doubtless he could not be termed an adverse claimant in possession. But that he could summarily be deprived of his right of possession were there such a dispute or lack of tender is exceedingly doubtful.

§ 1674. **Stock Exchange Not Contesting Sale of Bankrupt's Seat Not "Adverse Claimant."**—A stock exchange holding the proceeds of sale of a bankrupt member's seat is not an adverse claimant, and will be considered to be holding for the bankruptcy court, where it does not contest the right to transfer the seat.⁴⁸

§ 1675. **Mortgagees in Actual Possession "Adverse Claimants."**—Mortgagees who have taken actual possession before the filing of the

46. In *re Muncie Pulp Co.*, 14 A. B. R. 70, 139 Fed. 546 (C. C. A. N. Y.), distinguished in *In re Watertown Paper Co.*, 22 A. B. R. 190, 169 Fed. 252 (C. C. A. N. Y.). But compare, § 1692.

47. In *re Pratesi*, 11 A. B. R. 319, 126 Fed. 588 (D. C. Del.). But compare, § 1692.

48. *Odell v. Boyden*, 17 A. B. R. 756, 150 Fed. 731 (C. C. A. Ohio).

Pledgor of Certificate of Membership in Board of Trade, Query.—It has been held that the pledgor of a certificate of membership in a Board of Trade or Exchange or other similar body cannot be required by the bankruptcy court to make written application to the Board of Trade for the posting and sale of the certificate although the certificate is in the trustee's hands as assets of the estate. In *re Silberhorn*, 5 A. B. R. 568, 105 Fed. 809 (D. C. Ills.). This decision seems out of harmony with the weight of authority.

It is difficult to see why a pledgor of property in the trustee's hands is not subject to the jurisdiction of the bankruptcy court for all proceedings requisite to the realization upon the trustee's interest in the pledged property.

But where the rules of the Stock Exchange provide for a committee to act as a tribunal to settle the rights and liens of creditors upon a member's seat such tribunal is one established by contract and its determinations will be respected subject, of course, to the usual rules regulating the relations of such tribunals to the regularly constituted courts of the land. In one case where a nonresident creditor had asserted his lien on a stock exchange seat and also held a lien on assets in another state, the bankruptcy court refused to enjoin. In *re Currie (Austin)*, 26 A. B. R. 345, 185 Fed. 263 (C. C. A. N. Y.).

petition in bankruptcy, are adverse claimants;⁴⁹ although summary process will lie where the possession thus taken is not exclusive of the bankrupt.⁵⁰ And in one case it has been held that the mortgagee is not an adverse claimant where the possession was taken before default.⁵¹

§ 1676. **Alleged Fraudulent Transferee in Possession, "Adverse Claimant."**—An alleged fraudulent transferee in possession, is an adverse claimant;⁵³ although the adverse claimant be the wife of the bankrupt;⁵⁴ or his daughter.⁵⁵ An alleged buyer on an executed sale before the bankruptcy also is an adverse claimant.⁵⁶

§ 1677. **Alleged Preferential Transferee in Possession, "Adverse Claimant."**—An alleged preferential transferee in possession is an "adverse claimant."⁵⁷

§ 1678. **Assignee of Bankrupt's Wages, "Adverse Claimant."**—An assignee of the bankrupt's wages, holding under an assignment of wages to be earned in the future, is an "adverse claimant," and may not be proceeded against summarily.⁵⁸

In *re Driggs*, 22 A. B. R. 621, 171 Fed. 897 (D. C. N. Y.): "So far as the assignees are concerned, I have no jurisdiction over them in this case, and the validity of their assignment must be determined by plenary suit."

§ 1679. **Lienholder and Secured Creditor as "Adverse Claimants."**—It has been questioned whether a lienholder as such is an adverse claimant;⁵⁹ but a lienholder in possession, or rather a lienholder where the bankruptcy court is not in possession, is an adverse claimant and is not

49. *Heath v. Shaffer*, 2 A. B. R. 98, 93 Fed. 647 (D. C. Iowa); In *re Buntrock Clothing Co.*, 1 A. B. R. 454 (D. C. Iowa); instance, In *re Blake*, 22 A. B. R. 612, 171 Fed. 298 (D. C. N. Y.); In *re Rathman*, 25 A. B. R. 246, 183 Fed. 913 (C. C. A. S. D.); In *re Tarbox*, 26 A. B. R. 437, 185 Fed. 985 (D. C. Mass.).

50. In *re Brooks*, 1 A. B. R. 531, 91 Fed. 508 (D. C. Vt.). Compare, In *re Jersey Island Packing Co.*, 14 A. B. R. 689, 138 Fed. 625 (C. C. A. Calif.).

Delivery of one key but retention of another, see ante, § 1146, note.

51. In *re Waterloo Organ Co.*, 9 A. B. R. 427, 118 Fed. 904 (D. C. N. Y.).

53. *Wall v. Cox*, 5 A. B. R. 727, 181 U. S. 244; *Hicks v. Knost*, 2 A. B. R. 153, 94 Fed. 625 (D. C. Ohio); *Cooney v. Collins*, 23 A. B. R. 840, 176 Fed. 189 (C. C. A. Mont.), quoted at § 1865; In *re Clifford D. Mills*, 25 A. B. R. 278, 179 Fed. 409 (D. C. N. Y.). Compare, In *re Knopf*, 16 A. B. R. 432, 144 Fed. 245 (D. C. S. C.).

54. In *re Grahs*, 1 A. B. R. 465 (Ref. Ohio); In *re Tarbox*, 26 A. B. R. 432,

185 Fed. 985 (D. C. Mass.), quoted at § 1864. Compare, apparently to such effect, In *re Norris*, 24 A. B. R. 444, 177 Fed. 598 (D. C. N. Y.).

55. In *re Cohn*, 3 A. B. R. 421, 98 Fed. 75 (D. C. N. Y.).

56. In *re Flynn & Co.*, 11 A. B. R. 318, 126 Fed. 442 (D. C. N. Car.).

57. *Hicks v. Knost*, 2 A. B. R. 153, 94 Fed. 625 (D. C. Ohio); In *re Adams*, 12 A. B. R. 367, 130 Fed. 788 (D. C. R. I.); *Bindseil v. Smith*, 5 A. B. R. 40 (N. J. Ct. Errors); In *re Eurich's Fort Hamilton Brewery*, 19 A. B. R. 798, 158 Fed. 644 (D. C. N. Y.); In *re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.).

58. In *re Karns*, 16 A. B. R. 843 (D. C. Ohio); In *re Lineberry*, 25 A. B. R. 164, 183 Fed. 338 (D. C. Ala.); *Copeland v. Martin*, 25 A. B. R. 268, 182 Fed. 805 (C. C. A. Ala.). But compare, In *re Home Discount Co.*, 17 A. B. R. 180, 147 Fed. 538 (D. C. Ala.).

59. (1841) In *re Christy*, 3 How. 292; (1841) *Norton v. Boyd*, 3 How. 426. See note to *Carter v. Hobbs*, 1 A. B. R. 215, 92 Fed. 594 (D. C. Ind.).

subject to the summary jurisdiction of the bankruptcy court.⁶⁰ Thus, where a bankrupt has assigned his future earned wages both the assignee and employer are adverse claimants, not subject to the summary jurisdiction of the bankruptcy court.⁶¹

Likewise, sureties in possession of deposits made within the four months by the bankrupt for indemnity have been held to be adverse even after exoneration of the bankrupt, if the sureties claim a lien or other interest in the fund.⁶²

Again, the sister of the bankrupt is an adverse claimant where she holds as security a bond for title to real estate which her brother had transferred to her after having deeded the property to a third person for a loan, taking the bond in return.⁶³

But a liveryman, holding possession at the time of the bankruptcy under his lien, has been held subject to the summary jurisdiction of the bankruptcy court.⁶⁴

It has been held that an attorney holding chattel mortgages belonging to the bankrupt, upon which he claims an attorney's lien for services performed before the bankruptcy, is within the summary jurisdiction of the bankruptcy court;⁶⁵ but this is doubtless based upon the general doctrine that all courts have summary jurisdiction over attorneys practicing before them as regards their relations with their clients.

§ 1680. Debtors of Bankrupt "Adverse Claimants," Not to Be Proceeded against Summarily.—Debtors of the bankrupt are adverse claimants and may not be proceeded against summarily.⁶⁶

§ 1681. Thus, Banks Owning "Deposits," "Adverse Claimants."—Thus, banks holding deposits of the bankrupt are debtors, and therefore adverse claimants not subject to summary jurisdiction. Nevertheless, they

60. *Fitch v. Richardson*, 16 A. B. R. 535, 147 Fed. 196 (C. C. A. Mass.). In *re Blake*, 22 A. B. R. 612, 171 Fed. 298 (D. C. N. Y.); *Harris, trustee, v. Nat. Bank*, 216 U. S. 382, 23 A. B. R. 632; In *re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.). Apparently contra, In *re Cobb*, 3 A. B. R. 129, 96 Fed. 821 (D. C. N. C.).

61. In *re Karns*, 16 A. B. R. 841 (D. C. Ohio).

62. In *re Horgan*, 21 A. B. R. 31, 164 Fed. 415 (C. C. A. Mass.).

63. In *re Pickens & Bro.*, 26 A. B. R. 6, 184 Fed. 134 (D. C. Ga.), although in this case it does not appear who had actual possession of the real estate, the facts as to which would have settled the question of jurisdiction.

64. In *re Pratesi*, 11 A. B. R. 319, 126 Fed. 588 (D. C. Del.): However, this could not be the law unless the lienor in possession were tendered the amount of his lien, in which event the proceed-

ings would amount to a proceedings to redeem.

65. In *re Eurich's Fort Hamilton Brewery*, 19 A. B. R. 798, 158 Fed. 644 (D. C. N. Y.). See also, post, § 1823½, and § 2099.

66. In *re Manning*, 10 A. B. R. 497, 123 Fed. 180 (D. C. S. C.); In *re Zotti*, 23 A. B. R. 812, 178 Fed. 304 (D. C. N. Y.), as quoted at § 1681; In *re Zotti*, 26 A. B. R. 234, 186 Fed. 84 (C. C. A. N. Y., affirming S. C., 23 A. B. R. 304, 178 Fed. 304); In *re Boston-Cerrellos Corporation*, 30 A. B. R. 739, 206 Fed. 794 (D. C. N. Mex.); In *re Howe Mfg. Co.*, 27 A. B. R. 477, 193 Fed. 524 (D. C. Ky.).

Compare, rightly decided on the facts but wrongly reasoned, the court unnecessarily discussing the question of colorability as if summary process might otherwise have been proper. *First Nat. Bk. v. Hopkins*, 29 A. B. R. 434, 199 Fed. 877 (C. C. A. Ga.).

have frequently been summarily ordered to pay over funds and usually have not resisted where there have been no complications.⁶⁷

In *re Zotti*, 23 A. B. R. 812, 178 Fed. 304 (D. C. N. Y.), reversing S. C., 23 A. B. R. 601, affirmed in *In re Zotti*, 26 A. B. R. 234, 186 Fed. 84 (C. C. A.): "The bankrupt's property was the chose in action against the bank; to speak of it as 'money on deposit' is confessedly a colloquialism. * * * Here the bank has not meddled with the bankrupt's assets at all. The property was, as I have said, a chose in action to which it was an incident that the obligor should honor sight drafts. It did honor such a draft, innocently, as all sides concede, and in so doing it availed itself of the conditions of the very obligation under which the trustee now sues. Of course the trustee is subject to the same conditions when he sues as the bankrupt is under; one of these conditions is the right of the debtor bank to treat as a valid extinguishment pro tanto any payment made upon cheque. It is only by what seems to me a confusion of the fundamental relation between the bank and the bankrupt that I can hold liable the former. The bank in no sense transferred property of the bankrupt for it had no such property. He himself, the bank's customer, alone had any property, and that was a right to sue, subject to a condition which has occurred. I can only conclude that the order was erroneous and it must be reversed."

First Nat. Bank v. Hopkins, 29 A. B. R. 434, 199 Fed. 877 (C. C. A. Ga.): "The amount named in the judge's order, and which the bank was directed to pay over at once to the trustee, was on deposit in the bank to the credit of the Montgomery Drug Company when bankruptcy proceedings were instituted against that company. The bank held notes against the Montgomery Drug Company for a larger amount than the Drug Company's total deposits, and claimed the right to set off the notes against the deposits. The objection to this on the part of the trustee for the Montgomery Drug Company was that nearly all of the deposits standing to the credit of the Montgomery Drug Company in the bank had been deposited under a special arrangement, by which it was put there for the benefit of all the creditors of the Drug Company, to be paid to them on their debts, pro rata, and that the bank officers had notice that such was the character of the deposits.

"This was the matter at issue between the parties—that is, between the trustee in bankruptcy and the bank—when this summary proceeding was instituted. The deposits were entered on the books of the bank to the credit of the Montgomery Drug Company, and were ordinary deposits put by the bank on the Drug Company's deposit book. There was nothing whatever on the books of the bank to show that it was anything other than an ordinary deposit. The proceeds of a note given to the Montgomery Drug Company, for the purchase of its goods, amounting to \$10,000, and put to the credit of the Montgomery Drug Company, constituted the greater part of the deposits at the time of the institution of the bankruptcy proceedings.

"We must determine, therefore, on the facts of the present case, before going into it further, whether there was a real adverse claim on the part of the bank, without reference to what its merits might be when heard and determined, or whether it was merely colorable. It is perfectly clear to us that the claim of the bank in this case was a real adverse claim, and not merely colorable."

⁶⁷. Instance, *In re Grive*, 18 A. B. R. 202, 151 Fed. 711 (D. C. Conn.); *In re Boston-Cerellos Corporation*, 30 A. B. R. 739, 206 Fed. 794 (D. C. N. Mex.);

In re Gill, 26 A. B. R. 883, 190 Fed. 726 (C. C. A.); *In re Zotti*, 26 A. B. R. 234, 186 Fed. 84 (C. C. A. N. Y., affirming S. C., 23 A. B. R. 304, 178 Fed. 304).

§ 1682. Likewise, Owner Owing on Building Contract, Subject to Mechanic's Liens, "Adverse Claimant."—The owner of property, owing a balance on a building contract, subject to mechanics' and subcontractors' liens, is an adverse claimant.⁶⁸

Obiter, impliedly, *In re Adams*, 18 A. B. R. 181 (D. C. N. Y.): "* * * but inasmuch as the attorney for the bankrupt, who has prosecuted the mechanic's lien action has an attorney's lien for services therein, and inasmuch as the rights in that action cannot be adjudicated in the bankruptcy proceedings, except as the matter is brought into the bankruptcy court by consent, etc."

§ 1683. Also, Employers Holding Wages of Bankrupt Tied Up by Assignment, "Adverse Claimants."—Employers holding wages of the bankrupt tied up by assignments are adverse claimants, and may not be proceeded against summarily.⁶⁹

§ 1683¼. Sureties and Others Holding Deposits as Indemnity, "Adverse Claimants."—Sureties holding deposits as security are adverse claimants, not subject to summary order.⁷⁰

And this is so after their exoneration from liability on the bond if they still claim a lien for expenses, etc.⁷¹

The rule is the same where a bankrupt has deposited money to secure the release of a third party's property, where both he and the third party go into bankruptcy.⁷²

§ 1683½. Attorney of Bankrupt Paid in Advance, Whether "Adverse Claimant."—An attorney for a bankrupt, who has received payment to an unreasonable amount for services to be rendered in bankruptcy, doubtless is an "adverse claimant;" but the Act in § 60d gives summary jurisdiction to the bankruptcy court to re-examine the transaction and de-

68. Impliedly, *In re Grissler*, 13 A. B. R. 508, 136 Fed. 754 (C. C. A. N. Y.); *In re Greater Am. Exposition*, 4 A. B. R. 486, 102 Fed. 986 (C. C. A. Neb.). Compare, as to effect of consent to jurisdiction, *In re Huston*, 7 A. B. R. 92 (Ref. N. Y.).

But compare, *In re Hobbs & Co.*, 16 A. B. R. 544, 145 Fed. 511 (D. C. W. Va.), where the court seems to consider the power conferred in general terms upon the bankruptcy court by § 2 (6) to "bring in and substitute additional persons or parties in proceedings in bankruptcy when necessary for the complete determination of a matter in controversy" empowers the bankruptcy court to compel mechanics and materialmen holding subcontractor's liens to come into the bankruptcy proceedings and set up their liens, else "this court could not require the owner to pay over to its receivers or trustee the sum due. * * *" But the court in this case overlooks the jurisdictional obstacle

that lies at the very threshold: the court even when the lienholders come in would have no power to "require" the owners to pay their debts into the bankruptcy court. The obligation of the owner is a mere debt—to pay the contract price, and mere debts as we have seen the bankruptcy court cannot "require" to be paid into its registry by either plenary or summary process.

Also, see ante, § 1165, and post, § 1692.

69. Inferentially, *In re Driggs*, 22 A. B. R. 621, 171 Fed. 897 (D. C. N. Y.), quoted at § 1678.

70. *Jacquith v. Rowley*, 9 A. B. R. 525, 188 U. S. 620; *In re Horgan*, 19 A. B. R. 857, 158 Fed. 774 (C. C. A. Mass.); *In re Horgan*, 21 A. B. R. 31, 164 Fed. 415 (C. C. A. Mass.).

71. *In re Horgan*, 21 A. B. R. 31, 164 Fed. 415 (C. C. A. Mass.).

72. *In re Squier*, 21 A. B. R. 346, 165 Fed. 515 (D. C. N. Y.).

termine any excessiveness. As to this apparent exception, it is to be observed, first, that courts have always assumed summary jurisdiction over their officers and attorneys for the sake of preserving purity in the administration of justice; and, second, that, doubtless, the re-examination would not result in a summary order on the attorney to repay the excess if the attorney were shown to be unable to respond or were a non-resident. In these latter contingencies, the trustee would be obliged, doubtless, to sue for a judgment in a court whose judgment could be executed. In such suit, however, the order of the bankruptcy court determining the excess would be binding and final upon the parties.⁷³

DIVISION 2.

IN WHAT COURTS MAY PLENARY ACTIONS AGAINST ADVERSE CLAIMANTS BE BROUGHT BY TRUSTEES AND RECEIVERS IN BANKRUPTCY.

§ 1684. Plenary Suits against "Adverse Claimants" in State Courts.—Plenary suits against adverse claimants always may be brought in the State court, or the United States district court, that would have had jurisdiction of the parties had not bankruptcy intervened.⁷⁴

Andrews v. Mather, 9 A. B. R. 301, 134 Ala. 358: "Section 23 does not purport to take away any jurisdiction in law or equity which would otherwise exist in the United States Circuit [now District] or State Courts."

§ 1685. Distinction between Proceedings in Bankruptcy and "Controversies" Arising Out of Bankruptcy.—The distinction between proceedings in bankruptcy and controversies arising in bankruptcy proceedings is elsewhere elucidated.⁷⁵

⁷³. See post, § 2099.

⁷⁴. Bankr. Act, § 23 (b): "Suits by the trustee shall only be brought or prosecuted in the courts where the bankrupt, whose estate is being administered by such trustee, might have brought or prosecuted them if proceedings in bankruptcy had not been instituted, unless by consent of the proposed defendant, except suits for the recovery of property under section sixty, subdivision b, and section sixty-seven, subdivision e."

Bankr. Act, § 23 (a): "The United States circuit courts shall have jurisdiction of all controversies at law and in equity, as distinguished from proceedings in bankruptcy between trustees as such and adverse claimants concerning the property acquired or claimed by the trustee, in the same manner and to the same extent only as though bankruptcy proceedings had not been instituted and such contro-

versies had been between the bankrupts and such adverse claimants."

Bankr. Act, § 70 (e): "The trustee may avoid any transfer by the bankrupt of his property which any creditor of such bankrupt might have avoided, and may recover the property so transferred, or its value, from the person to whom it was transferred, unless he was a bona fide holder for value prior to the date of the adjudication. Such property may be recovered or its value collected from whoever may have received it, except a bona fide holder for value. For the purpose of such recovery any court of bankruptcy as hereinbefore defined, and any State court which would have had jurisdiction if bankruptcy had not intervened, shall have concurrent jurisdiction."

Frank v. Vollkommer, 17 A. B. R. 808, 205 U. S. 521; *Hobbs v. Frazier*, 26 A. B. R. 887 (Sup. Ct. Fla.).

⁷⁵. Post, § 2864.

Bankruptcy proceedings proper are those concerned with the adjudication of the debtor as a bankrupt and his discharge, and also such as concern the election of the trustee by creditors, the sale of assets belonging to the bankrupt estate, and the allowance of creditors' claims, and the distribution of the proceeds to creditors. The bankruptcy court has exclusive jurisdiction of such proceedings. "Controversies" "arising in bankruptcy proceedings," on the other hand, are all other bankruptcy controversies than those mentioned, arising with regard to property in the possession of the bankruptcy court or perhaps (though this point is not settled) with regard to property not in its possession. As to the former, the bankruptcy court in the bankruptcy proceedings themselves has jurisdiction, equally as well as in bankruptcy proceedings proper. Of the latter, the bankruptcy court has no summary jurisdiction whatever, and has only such plenary jurisdiction as is conferred by the Amendment of 1903, to recover property fraudulently or preferentially conveyed.⁷⁶

Compare, *Brumley v. Jones*, 15 A. B. R. 581, 141 Fed. 318 (C. C. A. Ga.): "The District Court does not possess the general power to entertain a suit in equity, and, unless the Bankrupt Act has conferred upon it jurisdiction to entertain a plenary suit in equity, such a suit cannot be maintained. * * * The bankrupt act confers on the District Courts, as courts of bankruptcy, such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in bankruptcy proceedings. As courts of bankruptcy they are vested with power to collect, reduce to money, and distribute the estates of bankrupts, and to determine controversies in relation thereto. * * * We think it clear that the controversies referred to relate to the collection, sale, and distribution of such estates. The jurisdiction of the District Court, as granted by the Bankruptcy Act, is unquestionably bankrupt jurisdiction, and not general jurisdiction to hear and determine controversies between adverse third parties, which are not strictly and properly a part of the bankruptcy proceedings."

§ 1686. Jurisdiction of United States District Court in Bankruptcy Matters.—The Bankruptcy Act, by § 23 (a) does not enlarge the jurisdiction of the United States District [formerly the Circuit] Courts. They would only have jurisdiction over suits brought by trustees in bankruptcy in case diversity of citizenship or some other jurisdictional fact existed, which, in the usual procedure, would have conferred jurisdiction on the District [formerly the Circuit] Court of the United States in case the bankrupt had sued;⁷⁷ nor unless the amount involved exceeds

⁷⁶. Compare, *Burleigh v. Foreman*, 11 A. B. R. 74, 125 Fed. 217 (C. C. A. Mass.); *McNulty v. Feingold*, 12 A. B. R. 338, 129 Fed. 1001 (D. C. Penn.); *Bank v. Title & Trust Co.*, 14 A. B. R. 102, 198 U. S. 280; *Delta Nat'l Bk. v. Easterbrook*, 13 A. B. R. 338, 133 Fed. 521 (C. C. A. Tex.). Compare, *In re Walsh Bros.*, 21 A. B. R. 14, 163 Fed. 352 (D. C. Iowa).

⁷⁷. *Bear Gulch, etc., Co. v. Walsh*, 28 A. B. R. 724, 198 Fed. 351 (D. C. Mont.); *Chattanooga Nat'l Bk. v.*

Rome Iron Co., 3 A. B. R. 582, 99 Fed. 82 (U. S. C. C. Ga.); *Goodier v. Barnes*, 2 A. B. R. 328, 94 Fed. 798 (C. C. U. S.); *In re Rochford*, 10 A. B. R. 608, 124 Fed. 182 (C. C. A. S. Dak.); *In re Reynolds*, 13 A. B. R. 249, 133 Fed. 584 (D. C. Mont.); *Viquesnay v. Allen*, 12 A. B. R. 406, 131 Fed. 21 (C. C. A. W. Va.). *Obiter*, *Goodnough Mercantile & Stock Co. v. Galloway*, 19 A. B. R. 244, 156 Fed. 504 (D. C. Ore.); *In re MacDougall*, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.). Also, see *Spencer*

\$2,000;⁷⁸ and even "consent" cannot confer jurisdiction upon the District [formerly Circuit] Court in bankruptcy cases, unless diversity of citizenship, etc., exists.⁷⁹

But the "diversity of citizenship" relates to the bankrupt's citizenship, not to the trustee's citizenship:

Bush v. Elliott, 202 U. S. 477, 15 A. B. R. 661: "That is, while the jurisdiction of the courts was not to be extended because of the bankruptcy proceedings or the citizenship of the trustee, it was preserved to the trustee in the jurisdiction where the bankrupt might have brought or prosecuted the suit but for the bankruptcy proceedings. While this section preserves the jurisdiction of the United States Circuit Courts [now District] over cases coming within clause a, in clause b the right of suit by the trustee is limited to courts wherein the bankrupt might have brought or prosecuted the action had the bankruptcy proceedings not been instituted. * * *

"The action in the present case was to recover a sum of money alleged to have been due, prior to the bankruptcy proceedings, to the Southern Car and Foundry Company, which was a citizen of the State of New Jersey. The amount involved and the diverse citizenship of the parties were such that the car company might have sued the defendant, a citizen of the State of Alabama, in the Circuit Court of the United States independently of the bankruptcy proceedings. We think, by the terms of this section, it was intended to preserve this right to the trustee in bankruptcy, and that the citizenship of the trustee is wholly immaterial to the jurisdiction of such a case."

Thus, the Circuit [now District] Court has been held to have jurisdiction of an action by a trustee in bankruptcy to recover usurious interest paid by the bankrupt to a national bank.

Reed v. American-German Nat. Bank, 19 A. B. R. 140, 155 Fed. 233 (U. S. C. C. Ky.): "The provision of this section which is particularly material is, therefore, that part of clause 'b' which enacts that suits by the trustee shall only be brought in the courts 'where the bankrupt * * * might have brought or prosecuted them if proceedings in bankruptcy had not been instituted.' If the bankruptcy proceeding had not been instituted, could the saddlery company have brought suit in this court to recover the usurious interest paid to defendant; it being a national banking association organized under a law of the United States, viz, the national act? This seems to be

v. Duplan Silk Co., 11 A. B. R. 563, 191 U. S. 526; for rules as to jurisdiction and rights of appeal and review in such cases.

No Judicial Cognizance of Record in the Bankruptcy Proceedings.—It was formerly held before the abolition of Circuit Courts and the transfer of their jurisdiction to District Courts that where the suit was brought in the United States Circuit Court, that court would not take judicial cognizance of the records of the United States District Court in the bankruptcy proceedings. *McDonald v. Clearwater Ry. Co.*, 21 A. B. R. 182, 164 Fed. 1007 (U. S. C. C. Idaho). Whether the District Court as such

will now take judicial cognizance of its records while sitting in bankruptcy has not been decided.

78. *Swafford v. Cornucopia Mines*, 15 A. B. R. 564, 140 Fed. 957 (U. S. C. C. Ore.). And deficiency in amount cannot be helped out by the addition of a statutory allowance for attorney's fees allowable on recovery.

79. *Contra*, *In re Seebold*, 5 A. B. R. 358, 105 Fed. 910 (C. C. A. La.). *Obiter*, *In re MacDougall*, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.).

McEldowney v. Card, 27 A. B. R. 937, 193 Fed. 475 (C. C. Tenn.); *Lovell v. Newman & Son*, 29 A. B. R. 482, 227 U. S. 412; *Mayer v. Cohrs.*, 26 A. B. R. 695, 188 Fed. 443 (C. C. Wash.).

the statutory test established for such cases in which, and in those described in the clause of the section which we have italicized and which was added by the Amendment of 1903, the right of the trustee to sue in the Federal courts does not depend upon the consent of the person sued, though in other cases it does. * * * Under the judiciary act, jurisdiction is given generally to the Circuit Courts of the United States [now District] of cases arising under the laws of the United States. The national banking act itself, as amended, gives the Circuit Courts concurrent jurisdiction with the courts of the State having jurisdiction in similar cases of suits to recover interest knowingly collected at a higher rate than allowed by law; and, if this were all, it might well be held that the judiciary act and the national banking act, when construed together, give this court jurisdiction of a case like this. But, as the plaintiff here derives his powers and rights as trustee from the Bankruptcy Act of 1898, it has seemed to the court that his right to sue must also be tested by the provisions of that act. As we have seen, § 23b of the Bankruptcy Act gives him the right to sue here if the saddlery company could have done so, had there been no bankruptcy proceeding. The saddlery company would have had that right, as the claim exceeds \$2,000 and arises under the laws of the United States. This court, therefore, has jurisdiction, and the demurrer must be overruled, both because the plaintiff has capacity to sue and because the court has jurisdiction of the action."

But the district [formerly circuit] court will not be permitted, even by the express order of the bankruptcy court, to carry on controversies over assets in the custody of the bankruptcy court.⁸⁰

Drew v. Myers, 22 A. B. R. 656, 81 Neb. 750, 116 N. W. 781: "It is plain from the reading of these sections that, if this action was to avoid a preference or to recover property fraudulently conveyed by the bankrupt, the state court would have concurrent jurisdiction with the Federal court of the same. Of all other actions brought by the trustee to recover property belonging to the bankrupt the State court retains sole jurisdiction." The rule is not quite broadly enough stated here. The Federal court also would have jurisdiction of suits to set aside any transfer which any creditor might have maintained had there been no bankruptcy.

The United States district [formerly circuit] court has no jurisdiction of a bill in equity the purpose of which is to control the distribution of a fund belonging to an estate in bankruptcy, and in the possession of the trustee thereof; nor does the fact that such a suit was begun in the district [formerly circuit] court with leave of the court of bankruptcy confer such jurisdiction.⁸¹

§ 1687. Jurisdiction of State Courts in Bankruptcy Matters.—Therefore, as a rule, the state court would be the one to which the trustee would be relegated, were it not for still further exceptions found in § 23 (b) and in § 70e, later discussed.

Thus, even since the Amendment of 1903, the state court has been a

^{80.} *Bray v. U. S. Fidelity & Guaranty Co.*, 22 A. B. R. 363, 170 Fed. 639 (C. C. A. W. Va.).

^{81.} *United States Fidelity Co. v. Bray*, 28 A. B. R. 207, 225 U. S. 205.

proper forum.⁸² Indeed, before the Amendment of 1903 the state courts alone possessed such jurisdiction except where diversity of citizenship conferred jurisdiction on the federal circuit [nor district] courts.^{82a}

The state court is not debarred from jurisdiction over suits against adverse claimants by any of the provisions of the Act.⁸³

Frank v. Vollkommer, 205 U. S. 521, 17 A. B. R. 808: “* * * the Amendment gave the bankruptcy court concurrent and not exclusive jurisdiction.”

And where rights conferred by the peculiar provisions of the Bankruptcy Act are involved, such rights are cognizable in the state court and the state court will enforce the Bankrupt Law wherever applicable.⁸⁴

Heath v. Shaffer, 2 A. B. R. 102, 93 Fed. 647 (D. C. Ia.): “If, upon the hearing, the State Court holds and adjudges the plaintiff's claim or lien to be invalid and void either at the common law or under the provisions of the Bankrupt Act, that court would, undoubtedly, order the property to be delivered to the possession of the trustee. If the State court holds and adjudges the lien of the plaintiff to be valid, it would, upon the proper showing, also recognize the title and rights of the trustee subject to the lien of the plaintiff and would enforce the same according to the true intent and meaning of the Bankrupt Act. In some of the discussions had upon this general subject, it seems to be assumed that the State courts cannot aid in carrying out the general provisions of the Bankrupt Act, and that the trustee can only appeal to the courts of bankruptcy when seeking to secure a disposition of a bankrupt's estate under that act; but this is a mistaken view of the law. The State courts, in all proceedings pending before them, have the right to apply and enforce the provisions of the Bankrupt Act in the determination of the questions at issue before them, and can give full protection to the rights of the trustee. The Bankrupt Act is the law of the land, and the State Courts have full right to enforce its mandates in all proceedings properly before them. Of course, it is not meant by this that a State court can adjudge a person to be bankrupt, or grant him a discharge, or control the distribution of the bankrupt's estate; but what is meant is that in all suits pending before them, wherein may be involved a contest between the trustee and a third party, which depends, in whole or in part, upon the provisions of the Bankrupt Act, the State Court must of necessity have full right and jurisdiction to apply and enforce the provisions of the Bankrupt Act,

⁸². Instance, *Breckons v. Snyder*, 15 A. B. R. 112, 211 Penn. St. 176; *Lawrence v. Lowrie*, 13 A. B. R. 297, 133 Fed. 995 (D. C. Penn.); *Pond Trustee v. N. Y. Exch. Bk.*, 13 A. B. R. 343, 124 Fed. 991 (D. C. N. Y.).

^{82a}. See ante, § 1653.

⁸³. *Small v. Muller*, 8 A. B. R. 449, 67 N. Y. App. Div. 143; *Mueller v. Bruss*, 8 A. B. R. 445, 112 Wis. 406; *Heath v. Shaffer*, 2 A. B. R. 102, 93 Fed. 647 (D. C. Iowa); *Andrews v. Mather*, 9 A. B. R. 301, 134 Ala. 358; *Silberstein v. Stahl*, 4 A. B. R. 626 (N. Y. Sup. Ct.); *Sheldon v. Parker*, 11 A. B. R. 170, 66 Neb. 610; impliedly, *Breckons v. Snyder*, 15 A. B. R. 112, 211 Penn. St. 176.

⁸⁴. *Hull v. Hudson*, 26 A. B. R. 725

(Ch. Ct. Del.); *Carling v. Seymour L'b'r Co.*, 8 A. B. R. 41, 113 Fed. 483 (C. C. A. Ga.); *Savings Bk. v. Jewelry Co.*, 12 A. B. R. 781, 123 Iowa 432. In re *Lesser*, 3 A. B. R. 823, 110 Fed. 439 (D. C. N. Y., reversed on other grounds): “The obligations of the Bankruptcy Act are as binding upon that court as upon this.” See ante, § 1597.

Inferentially, obiter, In re *Dana*, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.), quoted at § 1597. But compare, in effect contra, *Read v. Wallace*, 21 A. B. R. 839, 145 Ala. 209, 40 So. 407, although perhaps this case goes simply to the extent that the action cannot be in equity, but must be at law.

not only in deciding the question of right at issue, but in securing to the parties the proper protection accorded to them under the act."

The conferring of jurisdiction upon state courts over federal bankruptcy questions is constitutional.⁸⁵ And where the trustee thus resorts to the state courts to recover property he is entitled to all remedies and relief that would be afforded any other party litigant under the same facts.⁸⁶

Bindseil v. Smith, 5 A. B. R. 40 (N. J. Ch. App. & Err.): "The appellant further insists that, as fraud in the transfer is not alleged, but merely illegality under the Bankrupt Act, a court of equity has no jurisdiction by common law, and such jurisdiction cannot be conferred on a State court by a Federal statute. Conceding that our own laws must point out which of our own courts is competent to afford a remedy in such cases, we think the relief prayed is properly sought in the Court of Chancery. The complainant seeks to compel the defendant to transfer the legal title of certain choses in action, which he now holds. Such a transfer requires the execution of a written instrument by the defendant for obtaining which the procedure in equity is more adapted than that in the courts of law. A judgment against the defendant for damages would not be an adequate remedy for the loss of claims against other persons, one of which is secured also by a lien on lands. The jurisdiction of a court of equity to decree the transfer of such writings is clear."

And, on the other hand, where the trustee thus resorts to the state court he is bound, as *res adjudicata*, by the final determination of the state court.⁸⁷

§ 1688. But by Amendment of 1903 Jurisdiction Conferred Also in Certain Cases upon Bankruptcy Courts.—By the Amendment of 1903 to §§ 23 (b) and 70 (e) jurisdiction was conferred also in certain cases upon the bankruptcy courts where formerly lacking. Section 60, subdivision (b), and § 67, subdivision (e), expressly referred to in the Amendment to § 23 (b), are the sections relating to the recovery of property preferentially and fraudulently conveyed, respectively, within the four months preceding the bankruptcy, whilst § 70 (e) provides that the trustee may avoid any transfer which any creditor might have avoided had not bankruptcy intervened; and all these sections, as separately amended, contain similar provisions that "For the purpose of such recovery any court of bankruptcy as hereinbefore defined, and any state court which would have had jurisdiction if bankruptcy had not intervened, shall have concurrent jurisdiction," although only § 60 (b) and § 67 (e) were expressly mentioned again, in the Amendment of 1903 to § 23 (b).⁸⁸

Lynch v. Bronson, 20 A. B. R. 409, 160 Fed. 139 (D. C. Conn.): "The amendment without doubt gives to this court concurrent jurisdiction with the State courts, without the consent of the proposed defendant of any suit which sets forth such facts as will bring it under either of the excepted subdivisions."

85. *French v. Smith*, 4 A. B. R. 785 (Minn. Sup. Ct.).

86. *Sheldon v. Parker*, 11 A. B. R. 152, 66 Neb. 610.

87. *In re Reynolds*, 13 A. B. R. 248, 133 Fed. 584 (D. C. Mont.).

88. *Hurley v. Devlin*, 17 A. B. R. 793, 149 Fed. 368 (D. C. Kans.); *Kraver v. Abrahams*, 29 A. B. R. 365, 203 Fed. 782 (D. C. Pa.); *In re Desmond*, 28 A. B. R. 158, 198 Fed. 581 (D. C. Ala.).

§ 1689. **Cases under § 70 (e) Included.**—In the Amendment of 1903 to § 23 (b), whereby jurisdiction was granted to the bankruptcy court over adverse claimants in certain cases, Congress by obvious inadvertence failed to include cases arising under § 70 (e); and it was denied in some cases that that amendment gave to the federal courts jurisdiction, without consent, to entertain suits by trustees in bankruptcy to set aside any transfer other than fraudulent or preferential transfers.⁸⁹

That construction, however, rendered senseless the addition of the amended words to § 70 (e).

"The trustee may avoid any transfer by the bankrupt of his property which any creditor of such bankrupt might have avoided, and may recover the property so transferred, or its value, from the person to whom it was transferred, unless he was a bona fide holder for value prior to the date of the adjudication. Such property may be recovered or its value collected from whomsoever may have received it, except a bona fide holder.

"For the purpose of such recovery any court of bankruptcy as hereinbefore defined, and any state court which would have had jurisdiction if bankruptcy had not intervened, shall have concurrent jurisdiction."

Though even before the Amendment of 1903 the bankruptcy court already had been held to have such jurisdiction by consent; and the true rule, even before the Amendment of 1910, was that cases under § 70 (e) were also included.⁹⁰

But the question has been set at rest by the Amendment of 1910⁹¹ as follows:

Bankr. Act, § 23b, as amended in 1910: "Suits by the trustee shall only be brought or prosecuted in the courts where the bankrupt, whose estate is being administered by such trustee, might have brought or prosecuted them if proceedings in bankruptcy had not been instituted, unless by consent of the proposed defendant, except suits for the recovery of property under section sixty, subdivision b; section sixty-seven, subdivision e; and section seventy, subdivision e."

And now, proceedings under § 70 (e) for the recovery of property fraudulently transferred may be taken by the trustee without the defendant's consent in any court of bankruptcy where the defendant may be reached by process.⁹²

§ 1690. **Plenary Suits against "Adverse Claimants" in Bankruptcy Courts.**—Plenary suits against adverse claimants, then, can

89. *Obiter*, *Ryttenberg v. Schaefer*, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.); *Gregory v. Atkinson*, 111 A. B. R. 495, 127 Fed. 183 (D. C. Mo.); *Hull v. Burr*, 18 A. B. R. 541, 153 Fed. 245 (C. C. A. Fla.); *obiter*, *Drew v. Myers*, 22 A. B. R. 656, 81 Neb. 750; *Palmer v. Roginsky*, 23 A. B. R. 358, 175 Fed. 883 (D. C. N. Y.); *Skewis v. Barthell*, 18 A. B. R. 429, 152 Fed. 534 (D. C. Iowa); compare, *obiter*, *Harris v. Bank*, 216 U. S. 382, 23 A. B. R. 632;

Wood v. Lumber Co., 29 A. B. R. 220, 226 U. S. 384 (instituted prior to Amendment of 1910); *Sheppard v. Lincoln*, 25 A. B. R. 804, 184 Fed. 182 (D. C. N. Y.).

90. *Hurley v. Devlin*, 17 A. B. R. 797, 149 Fed. 268 (D. C. Kans.).

91. *Newcomb v. Biwer*, 29 A. B. R. 15, 199 Fed. 529 (D. C. So. Dak.).

92. *Parker v. Sherman*, 28 A. B. R. 379, 201 Fed. 155 (D. C. Vt.).

also be brought in bankruptcy courts, that is to say, in the district courts of the United States sitting in bankruptcy, whenever the trustee is attempting therein to set aside, 1st, a preference;⁹³ or 2nd, a fraudulent transfer made within the four months preceding the bankruptcy;⁹⁴ or 3rd, is attempting to set aside any transfer that a creditor might have set aside had there been no bankruptcy.⁹⁵

Horskins v. Sanderson, 13 A. B. R. 102, 132 Fed. 415 (D. C. Vt.): "Jurisdiction over the subject matter seems to be given to this court as a court of bank-

93. *Delta Nat. Bk. v. Easterbrook*, 13 A. B. R. 338, 133 Fed. 521 (C. C. A. Tex.). *Obiter*, *Off v. Hakes*, 15 A. B. R. 700 (C. C. A. Ills.). *Bowman v. Alpha Farms*, 18 A. B. R. 700, 153 Fed. 38 (D. C. N. Y.); *Gregory v. Atkinson*, 11 A. B. R. 495, 127 Fed. 183 (D. C. Mo.); *Parker v. Black*, 16 A. B. R. 202, 143 Fed. 560 (D. C. N. Y.); *obiter*, *Drew v. Myers*, 22 A. B. R. 656, 81 Neb. 750, 116 N. W. 781. *Kraver v. Abrahams*, 29 A. B. R. 365, 203 Fed. 782 (D. C. Pa.); *Hills v. McKinniss Co.*, 26 A. B. R. 329, 188 Fed. 1012 (D. C. Ohio); *Grant v. National Bank of Auburn*, 28 A. B. R. 712, 197 Fed. 581 (D. C. N. Y.).

94. *McNulty v. Feingold*, 12 A. B. R. 338, 129 Fed. 1001 (D. C. Penn.): The court held, in this case that under § 67 (e) as amended in 1903, a trustee in bankruptcy might maintain in a United States District Court a suit in equity, for an accounting of money collected by defendants upon accounts fraudulently assigned to them by the bankrupts, though the face value of such accounts were known to the complainants.

Kraver v. Abrahams, 29 A. B. R. 365, 203 Fed. 782 (D. C. Pa.); *Hills v. McKinniss*, 26 A. B. R. 329, 188 Fed. 1012 (D. C. Ohio); *Grant v. National Bank of Auburn*, 28 A. B. R. 712, 197 Fed. 581 (D. C. N. Y.).

95. See post, § 1709; *Teague v. Anderson Hdw. Co.*, 20 A. B. R. 424, 161 Fed. 165 (D. C. Ga.); *obiter*, *Drew v. Myers*, 22 A. B. R. 656, 81 Neb. 750, 116 N. W. 781; *Frost v. Latham & Co.*, 25 A. B. R. 313, 181 Fed. 866 (C. C. Ala.); *Johnston v. Forsyth Mercantile Co.*, 11 A. B. R. 669, 127 Fed. 845 (D. C. Ga.): "Jurisdiction is concurrent with that of the State court and is here invoked to set aside a transfer on the part of an insolvent debtor, which it is alleged is declared to be null and void, as against the creditors of such debtor, by the law of the State. The amendment expressly confers jurisdiction by the proceedings in equity in a

District Court to set aside such conveyances."

Jurisdiction to Recover from Vendee of Bankrupt, Who Knew the Facts, Property Bought by Bankrupt Through Fraudulent Misrepresentations.—In one case it has been held that the trustee succeeds to the rights of defrauded sellers to pursue property bought by the bankrupt through fraudulent misrepresentations and by him retransferred to third persons who had full knowledge of the fraud, such defrauded sellers having proved their claims as creditors and thus waived the tort. *Lynch v. Bronson*, 20 A. B. R. 409, 160 Fed. 139 (D. C. Conn.). This holding is peculiar, however. It would seem that the right of such creditors was to have pursued the property themselves, and that by waiving the right they did not confer it on the trustee, but that the trustee must depend solely upon the fraudulent nature of the transfer as between *all* the bankrupt's creditors and the vendee, rather than as between these particular sellers and the vendee.

Jurisdiction Where Transfer after as Well as before Filing of Petition.—The bankruptcy court has jurisdiction in a plenary suit, independently brought, to recover property transferred after as well as before the filing of the petition and even where possession has been obtained by the adverse claimant from the bankruptcy receiver or trustee himself. *Whitney v. Wenman*, 14 A. B. R. 45, 198 U. S. 539.

Jurisdiction Where Property Surrendered by Bankruptcy Receiver without Authority.—Thus, it has jurisdiction in a plenary suit, to recover from an adverse claimant property surrendered to him by its own receiver (and probably also even if surrendered by the trustee) without authority of court and perhaps for other reasons, *Whitney v. Wenman*, 14 A. B. R. 45, 198 U. S. 539; but it has been held, that the bankruptcy court has not jurisdiction to do so by summary process in a case where the receiver was persuaded to

ruptcy by the amendments of 1903 to the bankruptcy law. It extends by the amendment of § 70 (e) * * * to the recovery of any property from any transfer which any creditor might have avoided; by that of § 60b * * * to the recovery of unlawful preferences; and by that of § 67e * * * to the recovery of property conveyed or transferred within the four months."

§ 1691. **Plenary Suits by Trustees Not "Proceedings in Bankruptcy," but "Controversies."**—Plenary suits by trustees are not "proceedings in bankruptcy," but are "controversies" arising out of bankruptcy proceedings.⁹⁶

§ 1692. **But When Not to Be Brought in Bankruptcy Court.**—But when the adverse claim is not by way of a preference, nor by way of a fraudulent transfer made within the four months preceding the bankruptcy, nor by way of a transfer by the bankrupt that would have been voidable at the suit of some creditor had there been no bankruptcy, the suit for recovery cannot be brought in the bankruptcy court, at all, unless by consent of the adverse claimant so in possession or unless possession has been obtained by him after bankruptcy from an officer of the bankruptcy court himself; but such suit must be brought in the state court or (where facts exist, by way of diversity of citizenship, etc., that would have operated,

surrender property voluntarily to an adverse claimant, *Moore v. Hinds*, 14 A. B. R. 1 (C. C. A. Tenn., reversing *Leeds Woolen Mills*, 12 A. B. R. 136, 129 Fed. 922.).

But that this is doubtful, see suggestive *quare*, *Whitney v. Wenman*, 14 A. B. R. 45, 198 U. S. 539.

And certainly such would be the rule if the surrender were procured collusively.

Query: Whether Where Summary Jurisdiction Exists, Plenary Jurisdiction Also Exists.—Probably it is the rule that wherever summary jurisdiction would exist in the bankruptcy court plenary jurisdiction, a fortiori, would also exist. Compare tenor of court's opinion, *Whitney v. Wenman*, 14 A. B. R. 45, 198 U. S. 539. Also, compare general tenor of the court's decision in *Rytenberg v. Schaefer*, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.).

Trustee Not Confined to Suing in Own District Court.—The trustee is not confined to suing in the same district court wherein the bankruptcy proceedings themselves are pending: he may go into districts and sue there, if jurisdiction otherwise exists. *Lawrence v. Lowrie*, 13 A. B. R. 297 (D. C. Penn.).

Nonresident Protected from Service

of Summons While in Attendance at Bankruptcy Court in Support of His Claim.—A nonresident is protected from the service of summons upon him in a suit brought by the trustee against him, while he is in attendance at the bankruptcy court in support of his claim as creditor. *Morrow v. Dudley & Co.*, 16 A. B. R. 459 (D. C. Penn.).

Trustee Not Confined to Suing in Own District Because of Adjudication Being Based on Service by Publication.—Adjudication upon service by publication is precisely as effective as upon personal service, and the trustee is not confined to his own district in his suit to recover property. *Hills v. McKinniss*, 26 A. B. R. 329, 188 Fed. 1012 (D. C. Ohio).

96. *McNulty v. Feingold*, 12 A. B. R. 338, 129 Fed. 1001 (D. C. Penn.); *Delta Nat'l Bk. v. Easterbrook*, 13 A. B. R. 338, 133 Fed. 521 (C. C. A. Tex.); *Stelling v. Jones Lumber Co.*, 8 A. B. R. 521, 116 Fed. 261 (C. C. A. Wis.); *Boonville Nat'l Bk. v. Blakey*, 6 A. B. R. 13, 107 Fed. 891 (C. C. A. Ind.). Compare, *Bank v. Title & Trust Co.*, 14 A. B. R. 102, 198 U. S. 280; *In re Walsh Bros.*, 21 A. B. R. 14, 163 Fed. 352 (D. C. Iowa). See post, "Appeals and Error," §§ 2874, 2927.

in case bankruptcy had not intervened, to confer jurisdiction) may be brought in the United States District court.⁹⁷

Hull v. Burr, 18 A. B. R. 541, 153 Fed. 945 (C. C. A. Fla.): "Does the Amendment of 1903 affect the case at bar? The amendment makes exceptions to the limitation on the jurisdiction of the District Courts, and thereby extends their jurisdiction; but the extension does not include cases like that presented by the petition of the trustee. The amendment confers jurisdiction on the District Courts in 'suits for the recovery of property under section sixty, subdivision b, and section sixty-seven, subdivision e.' Turning to § 60, we find that subdivision 'a' defines a preference, and that subdivision 'b' provides that the trustee may sue the person receiving a preference and recover the property or its value. Under the amendment, suit for that purpose may be brought in 'any court of bankruptcy.' The case at bar involves no question of preference. Examining § 67, subd. 'e,' we find that it relates to fraudulent conveyances by the bankrupt and conveyances made within four months prior to the time of filing the petition in bankruptcy. The amendment confers jurisdiction on any court of bankruptcy of suits to recover property so conveyed. The petition of the trustee in the case at bar contains no charge of fraud, and the deed and contracts in question were executed more than four months before the beginning of the bankruptcy proceedings. It follows that the amendment quoted has no application to this case. The case, when viewed as a controversy at law or in equity, not being affected by the amendment, must be governed by the principles announced in *Bardes v. Hawarden Bank*, supra, which denies the jurisdiction of the District Court. The only other part of the act that might be referred to in this connection is § 70, subd. 'e.' * * * Such jurisdiction as is conferred by this language relates to suits by the trustee to 'avoid any transfer by the bankrupt of his property which any creditor of such bankrupt might have avoided.' The petition of the trustee in the instant case does not seek to avoid a transfer. It does not allege that the deed to Hull was made under circumstances that made it voidable at the suit of his creditors. In fact, it is not alleged in the petition that the corporation owed any debts at the date of its transfer to Hull. No charge of fraud against creditors is made. On the contrary, it is alleged that the deed to Hull was based on a large consideration, not less than \$25,000. A careful consideration of the trustee's petition convinces us that it was not intended as a suit under § 70e, and that subdivision has not been cited by learned counsel for the trustee as conferring jurisdiction. The trustee is vested by the act with all the rights and title of the bankrupt, as well as with the rights of the bankrupt's creditors, and, when he seeks to enforce rights or to recover property in another district outside of the territorial jurisdiction of the court which appointed him, he stands in the position of those whose rights he has acquired, and can resort only to the same courts, State or Federal, and is confined to the same remedies. * * * This general rule is, of course, subject to the exceptions made by the Amendment of 1903, which has been quoted in this opinion and shown not to be applicable to this case."

Drew v. Myers, 22 A. B. R. 656, 81 Neb. 750, 116 N. W. 781: "The State and Federal courts have concurrent jurisdiction of an action brought by a trustee

97. In *re Ratham*, 25 A. B. R. 246, 183 Fed. 913 (C. C. A. S. D.); impliedly, In *re Hutchinson & Wilmoth*, 19 A. B. R. 313, 158 Fed. 74 (C. C. A. Mich.), quoted at § 977; apparently, *Bank v.*

Title & Trust Co., 14 A. B. R. 102, 198 U. S. 280 (reversing 11 A. B. R. 79). See cases among those cited under main proposition of this chapter, ante, § 1652, et seq.

in bankruptcy to avoid a preference or to recover property, fraudulently conveyed by the bankrupt. Of all other actions brought by the trustee to recover property belonging to the bankrupt the State court has sole jurisdiction." The rule is not completely stated by this holding, however; for jurisdiction is also extended to the Federal Court over suits to set aside any transfer that a creditor might have set aside had there been no bankruptcy. However, the case itself was rightly decided, because it would appear that the suit was not brought to set aside a "transfer."

Thus, the title to property in the possession of an adverse claimant alleged to have been sold to him before the bankruptcy may not be tried out in the bankruptcy court; although, when the purchaser comes into the bankruptcy proceedings to present his claim, it may be diminished, or denied participation in dividends.⁹⁸ Thus, the owner of property holding a fund, or owing money, on a building contract subject to mechanics' or subcontractors' liens, may not be sued in the bankruptcy court.¹

A suit to recover damages for conspiracy may not be brought in the district court.² Thus, also, one who has seized the bankrupt's property wrongfully may not be sued by the trustee in the District Court of the United States for its recovery, unless the seizure was made within four months before the bankruptcy and was made by legal proceedings, or unless it amounted to a voidable preference. Nor may a suit be brought there against one who has obtained goods from the bankruptcy court, unless by his own consent to the jurisdiction, for his case does not come within any of the exceptions of the Statute: It is not a case of fraudulent conveyance within four months, nor a voidable preference, nor is it the result of a "transfer" by the bankrupt voidable by creditors. Nor may trust property belonging to the bankrupt, but never in his possession, nor "transferred" by him, be reached in the federal courts.

Nor may a suit to recover unpaid stock subscriptions be brought there;³ nor a suit to declare a trust in property, where no transfer by the bankrupt is alleged.⁴

Facts conferring jurisdiction on the federal court must be pleaded and proved; and it is not sufficient that they simply be pleaded,—the proof must support them.⁵

Suit may not be maintained in the District Court by the trustee to recover a leasehold interest claimed by the landlord to have been terminated by a

98. *In re Flynn & Co.*, 11 A. B. R. 318, 126 Fed. 422 (D. C. N. Car.).

1. Compare, inferentially, although before the Amendment, 1903, *In re Greater Am. Exposition*, 4 A. B. R. 486, 102 Fed. 986 (C. C. A. Tenn.). Ante, § 1682.

2. *Lynch v. Bronson*, 24 A. B. R. 513, 177 Fed. 605 (D. C. Conn.), quoted at § 1694.

3. See ante, § 977; also, see *In re Hutchinson & Wilmoth*, 19 A. B. R.

313, 158 Fed. 74 (C. C. A. Mich.); contra, *Skillin v. Magnus*, 19 A. B. R. 397, 162 Fed. 689 (D. C. N. Y.); also, contra, *In re Crystal Springs Bottling Co.*, 3 A. B. R. 194, 96 Fed. 945 (D. Ct. Vt.).

4. *Newcomb v. Biwer*, 29 A. B. R. 15, 199 Fed. 529 (D. C. So. Dak.); apparently, but obiter, *Drew v. Myers*, 22 A. B. R. 636, 81 Neb. 750, 116 N. W. 781.

5. *Plaut, trustee, v. Gorham Mfg. Co.*, 23 A. B. R. 42, 174 Fed. 852 (D. C. N. Y.).

judgment in dispossess proceedings, proof not showing the premises to be in the custody of the bankruptcy court.⁶

Thus, also, a secured creditor retaining security after, as it is claimed, the debt has been paid, may not be sued for its recovery in the Federal court.

Harris, trustee, *v.* Nat. Bank, 216 U. S. 382, 23 A. B. R. 632: "That subdivision [Bankr. Act, § 70e] provides for avoiding transfers of the bankrupt's property which his creditors might have avoided, and for recovery of such property, or its value, from persons who are not bona fide holders for value. In this action, no such transfer is alleged; no attack is made upon a transfer by the bankrupt which would have been void as to creditors. The petition seeks to recover property held by the bank, if the allegations are true, which belonged to the bankrupt, and consequently passed to the trustee as the representative of the bankrupt's estate. The recovery sought is of property held for the bankrupt estate, which the defendant wrongfully refused to surrender."

§ 1693. Third Parties Not to Resort to Bankruptcy Court Where Neither Property in Its Custody nor Either Party, Party to Bankruptcy Proceedings.—Nor may third parties resort to the bankruptcy court to litigate their rights there, where neither the bankruptcy court has custody of the property, nor either of the parties was a party to the proceedings in bankruptcy;⁷ nor any property is recoverable by general creditors.⁸

§ 1693½. Lienholders on Property in Custody of Bankruptcy Court Maintaining Plenary Suits in District Court.—It has been held that where the property is in the custody of the Bankruptcy Court a lienholder may institute an independent plenary action in the same District Court, to bring in the trustee and other parties and marshal the liens and for sale as in foreclosure, though not in terms a foreclosure.

Goodnough Mercantile & Stock Co. v. Galloway, 19 A. B. R. 244, 156 Fed. 504 (D. C. Ore.): "The relation of the parties in the case at bar is the exact reverse of that of those in that case [*Whitney v. Wenman*, 198 U. S. 539] but the principle involved appears to me to be the same. The purpose is to determine the validity of the alleged lien claimed upon the property of the bankrupt. The fund derived from the sale of the lumber and logs had passed into the hands of the trustee, and, although the contracts for the timber with the Lewises are in the hands of plaintiff by assignment as collateral, yet the corpus of the lien, to wit, the timber, whatever may be the interests of the bankrupt, has passed into the constructive possession, at least, of the trustee, so that the whole property is within the possession, actual or constructive, of the bankrupt court, and the suit is brought in that court, by the

6. *Plaut, trustee, v. Gorham Mfg. Co.*, 23 A. B. R. 42, 174 Fed. 852 (D. C. N. Y.). For no transfer by the bankrupt was involved, nor was there any consent to the jurisdiction, nor was the property in the custody of the Bankruptcy Court.

7. *Henrie v. Henderson*, 16 A. B. R. 621, 145 Fed. 316 (C. C. A. W. Va., reversing *In re Henderson*, 15 A. B. R. 760). See post, § 1700.

8. And only trustee, not creditors, may bring the plenary action in Bankruptcy Court. See post, §§ 1716 and 1718.

lienholder, to determine the correlative rights of the parties. The plaintiff does not in any way hold, or assume to hold, adversely to the trustee in bankruptcy, and I see no reason why a plenary suit may not be maintained by the lienholder against the trustee to determine those rights, as well as by the trustee against the lienholder. The suit is plenary in either case, and the court is in the possession of the property involved. That the case is in name one for a foreclosure does not in itself determine the jurisdiction. The court will not foreclose in the way that foreclosure proceedings are finally adjusted, but it will declare the lien, if any exists, and leave the trustee to dispose of the property, and the assets will be marshaled in accordance with the relative rights of the creditors of the estate; the legitimate lienholder being preferred, of course, to the general creditor. This disposes of the question of jurisdiction."

§ 1694. Actions in Personam for Debts Not to Be Brought in Bankruptcy Courts.—Likewise, actions for merely money judgments or for other relief in personam, where the court does not attempt to recover any property transferred by the bankrupt, nor its value, but merely to render judgment in personam for a debt or other obligation not arising from a transfer by the bankrupt, or to order specific performance of some contract or duty, may only be instituted against a debtor, or other third party, in the court in which the bankrupt himself, or his creditors had there been no bankruptcy, might have instituted them, and may not (except by consent) be instituted in the bankruptcy court.⁹

Bush v. Elliott, 202 U. S. 477, 15 A. B. R. 565: "The excepted suits, for the recovery of property, covered by the Amendment of 1903, pertain to actions to recover property conveyed by the bankrupt in fraud of the Act and do not concern actions of the character now under consideration. * * * to recover certain sums of money alleged to have been lent by the bankrupts for goods sold and delivered to the defendant and upon an account stated and for money paid for them by the bankrupt."

Hinds v. Moore, 14 A. B. R. 1, 134 Fed. 221 (C. C. A. Tenn., reversing *In re Leeds Woolen Mills Co.*, 12 A. B. R. 136, 129 Fed. 922): "The case is distinguishable in its facts and upon principle from *White v. Schloerb*. There has been no use of the writ of another court. There has been no taking by force or fraud. Neither is it possible to restore the goods themselves to the custody of the court. A money judgment for the value of the goods is the relief sought, and the only relief possible. To obtain that relief, the trustee concedes that the question of title and value must be tried out under a rule to show cause. * * * Confining ourselves to the case before us, we think the bankrupt court did not have jurisdiction to require the appellant to show cause why he should not pay to the bankrupt's estate the value of the goods so voluntarily surrendered by the referee to him. The court, having voluntarily parted with the custody of the goods, has not the jurisdiction to proceed summarily for their value.

9. Also, see instances among cases cited under the main proposition of this chapter, ante, § 1652, et seq.

Only in Cases Where Bankruptcy Occurred Since Amendment.—And such plenary suits cannot be brought in any case in the District Court of the United States unless they grow out of bankruptcy proceedings which were in-

stituted after the amendatory Act of 1903 took effect. That amendment was not retroactive. *In re Hartman*, 10 A. B. R. 387, 121 Fed. 940 (D. C. Mass.). *Contra*, *Pond v. N. Y. Exch. Bk.*, 10 A. B. R. 343, 124 Fed. 992 (D. C. N. Y.). Compare, *In re White (Froehling v. Amer. Trust & Savings Bank)*, 24 A. B. R. 197, 177 Fed. 194 (C. C. A. Ill.).

Thus, suits to recover unpaid stock subscriptions may not be brought there.¹⁰

And a suit to recover damages for conspiracy is not a suit to set aside a transfer nor to "recover" property, and therefore it may not be brought in the district court.¹¹

§ 1695. No Plenary Suits before Referee.—Plenary suits in no event can be brought in the referee's court;¹² for the referee, though included within the term "the court" by clause 7 of § 1 of the Act, has not the machinery at his disposal for carrying on a plenary suit, with its requirement of formal service of process, rule days, pleadings, trial and verdicts. A plenary suit brought by a trustee in bankruptcy is, as we have above seen, not a bankruptcy proceeding nor a proceeding in bankruptcy, although it is an action or a proceeding growing out of a bankruptcy proceeding. Referees seem to be restricted in their jurisdiction to purely bankruptcy proceedings, and also to such controversies arising out of bankruptcy proceedings as concern property within the possession or control of the bankruptcy court. They have no power to render judgments in personam.¹³

The plenary jurisdiction conferred by the Amendatory Act of 1903 upon courts of bankruptcy over property in certain specified cases, is not to be construed as stretching to the referees.¹⁴

10. See cases cited under § 1692.

11. *Lynch v. Bronson*, 24 A. B. R. 513, 177 Fed. 605 (D. C. Conn.): "As the matter now stands, however, the complaint appears to state nothing more nor less than a suit by reason of a conspiracy to recover damages. It is, therefore, in no sense within the provisions of § 67 (e)."

12. Compare, ante, § 545. See *In re Walsh Bros.*, 21 A. B. R. 14, 163 Fed. 352 (D. C. Iowa), quoted ante, § 1652; *In re Overholzer*, 23 A. B. R. 10 (Ref. N. Dak.); *Horskins v. Sanderson*, 13 A. B. R. 102, 132 Fed. 415 (D. C. Vt.); *In re Grahs*, 1 A. B. R. 465 (Ref. Ohio); *In re Scherber*, 12 A. B. R. 616, 131 Fed. 121 (D. C. Mass.); *In re Cohn*, 3 A. B. R. 421, 98 Fed. 75 (D. C. N. Y.).

Contra, *In re Shults & Marks*, 11 A. B. R. 690 (Ref. N. Y.): The referee in this case lays stress on the fact that "the case" was referred to him. The case referred to him, however, was not the independent suit of the trustee against the alleged preferential or fraudulent transferee but the bankruptcy proceedings themselves. All questions relating to the property actually or constructively in the custody of the court are within the referee's jurisdiction: questions relating to other property are not. Thus, property in the possession of a mere agent or one

not claiming to hold beneficial interest therein, is not adversely held, and so the referee's jurisdiction extends to such property.

Compare, *In re Steuer*, 5 A. B. R. 209, 104 Fed. 976 (D. C. Mass.). *Quære*, *In re Goldberg*, 1 A. B. R. 385 (Ref. Utah). But compare, when no objection to jurisdiction is made, obiter, *In re Scherber*, 12 A. B. R. 616, 131 Fed. 121 (D. C. N. Y.).

Also, compare, where it appears the referee was acting as an arbitrator, though evidently considering jurisdiction existed anyway, *In re O'Brien*, 21 A. B. R. 11 (Ref. Mass.).

Lack of Referee's Original Jurisdiction, Cured by Appeal without Original Objection.—And one case has held that where the jurisdiction of the referee was not objected to and the summary petition contained all the substantial allegations of a bill in equity, the judge on appeal had jurisdiction to order the return of the preference involved, whether the referee originally had jurisdiction or not. *In re Steuer*, 5 A. B. R. 209, 104 Fed. 976 (D. C. Mass.). But compare, *In re Scherber*, 12 A. B. R. 616, 131 Fed. 121.

13. *Knapp & Spencer v. Drew*, 20 A. B. R. 355, 160 Fed. 413 (C. C. A. Neb.). Compare, ante, § 545½.

14. *In re Overholzer*, 23 A. B. R. 10 (Ref. N. Dak.).

But, undoubtedly, if the property involved is placed within the control of the bankruptcy court, the referee has jurisdiction to try out its title and the rights of lienholders and others in it.

SUBDIVISION "A."

JURISDICTION BY CONSENT.

§ 1696. **Jurisdiction by Consent.**—Jurisdiction may be conferred on the bankruptcy court by the defendant's consent in cases wherein otherwise it has no jurisdiction, and if adverse claimants in possession of the property who would otherwise not be within the jurisdiction of the bankruptcy court, nevertheless voluntarily surrender custody of the property, or consent to the jurisdiction of the bankruptcy court, then the question of ownership and all other questions in relation thereto, as, for instance, the extent, validity and priority of liens upon and interests in the property, may be tried out in the bankruptcy proceedings.¹⁵

15. Bankr. Act, § 23 (b). *Obiter*, *Bryan v. Bernheimer*, 5 A. B. R. 631, 181 U. S. 188. *In re Hadden-Rodee Co.*, 13 A. B. R. 604, 125 Fed. 886 (D. C. Wis.).

In re Hymes Buggy & Implement Co., 12 A. B. R. 477, 130 Fed. 977 (D. C. Mo.), which was a case of voluntary surrender by a sheriff to the receiver in bankruptcy, the court holding that thereby the State Court was divested of jurisdiction and the bankruptcy court invested therewith.

In re Antigo Screen Door Co., 10 A. B. R. 359, 123 Fed. 249 (C. C. A. Wis.); *In re Riker*, 5 A. B. R. 720, 107 Fed. 96 (C. C. A. N. Y.). *Obiter*, *Ryttenberg v. Schaefer*, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.): This case is *obiter*, for the fund already was in the trustee's hands and thus in the custody of the court.

Obiter, *In re Fowler*, 1 A. B. R. 662, 93 Fed. 417 (Ref. Conn.); *In re Rochford*, 10 A. B. R. 608, 124 Fed. 182 (C. C. A. S. Dak.); *In re Steuer*, 5 A. B. R. 209, 104 Fed. 976 (D. C. Mass.); *In re Kolin*, 13 A. B. R. 531, 134 Fed. 557 (C. C. A. Ills.).

Inferentially (possession not being in the adverse claimant), *Chauncey v. Dyke Bros.*, 9 A. B. R. 444, 119 Fed. 1, 3 (C. C. A. Ark., affirming *In re Matthews*, 6 A. B. R. 96, 109 Fed. 603).

Stelling v. Jones Lbr. Co., 8 A. B. R. 521, 116 Fed. 261 (C. C. A. Wis.), which was a case of disputed possession and disputed title.

Boonville Nat'l Bk. v. Blakey, 6 A. B. R. 13, 107 Fed. 891 (C. C. A. Ind.);

Phillips v. Turner, 8 A. B. R. 171, 114 Fed. 726 (C. C. A. Miss.); *obiter*, *In re Andre*, 13 A. B. R. 132, 68 C. C. A. 374 (C. C. A. N. Y.); inferentially, *In re Bender*, 5 A. B. R. 632, 106 Fed. 873 (D. C. Ark.); *In re Porterfield*, 15 A. B. R. 11, 138 Fed. 192 (D. C. Va.).

Instance, *In re Rosenberg*, 8 A. B. R. 624, 116 Fed. 402 (D. C. Penn.), which was a case of an adverse claimant consenting and afterwards himself becoming bankrupt: his trustee was held bound by his consent, as well as that, both being in bankruptcy, the bankruptcy court acquires complete jurisdiction anyway.

Apparently, but unnecessarily, *Hatch v. Curtin*, 19 A. B. R. 82, 154 Fed. 791 (C. C. A. Mass.) although in this case no waiver nor consent was requisite since the bankrupt was in actual possession, though claiming to be holding simply as trustee for another.

Detroit Trust Co. v. Pontiac Sav. Bank, 27 A. B. R. 821, 196 Fed. 29 (C. C. A. Mich.); *Kilgore v. Barr*, 28 A. B. R. 860 (Ct. App. Va.).

"Consent" given as ground of jurisdiction though jurisdiction existing anyway. *In re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio).

But Not on United States District Court.—But consent will not confer jurisdiction on the United States District Court when it is not "sitting in bankruptcy," unless that court has jurisdiction over the subject matter as well. But see, analogously, *contra*, *In re Seebold*, 5 A. B. R. 358, 105 Fed. 910 (C. C. A. La.).

Obiter, Bardes v. Bank, 178 U. S. 524, 4 A. B. R. 163: "On the contrary, Congress, by the second clause of § 23 of the present Bankrupt Act, appears to this court to have clearly manifested its intention that controversies, not strictly or properly part of the proceedings in bankruptcy, but independent suits brought by trustees in bankruptcy to assert a title to money or property as assets of the bankrupt against strangers to those proceedings, should not come within the jurisdiction of the District Courts of the United States, 'unless by consent of the proposed defendant,' of which there is no pretence in this case."

In *re Blake*, 17 A. B. R. 668, 150 Fed. 279 (C. C. A. Mo.): "A court of bankruptcy may acquire by consent of all the parties in interest jurisdiction to determine a controversy between the trustee and an adverse claimant concerning an indebtedness of a third party and the lawful power to adjudicate all the claims of the parties thereto and to enforce their rights against each other by decree and execution."

In *re Connolly*, 3 A. B. R. 842, 100 Fed. 620 (D. C. Penn.): "Such conduct is certainly 'consent;' and, while it is usually true that consent cannot give jurisdiction, this is not universally true. The rule has no application when a statute clearly implies, as does section 23, that the jurisdiction of a certain class of controversies may be given by consent, for, in such event, to apply the rule would be to make the statute of no effect."

In *re Emrich*, 4 A. B. R. 89, 101 Fed. 231 (D. C. Penn.): "But in this case the license involved was already in the custody of the bankruptcy court."

Thus, consent may confer jurisdiction over a fund in the owner's hands subject to mechanic's liens;¹⁶ and over a fund in a trustee's or a stakeholder's hand.

Thus, also, where the ownership of a fund or debt is in dispute between the trustee and a third party, if the holder of the fund or the debtor pay the

¹⁶ In *re Huston*, 7 A. B. R. 92 (Ref. N. Y.). *Obiter*, inferentially, In *re Adamo*, 18 A. B. R. 181, 151 Fed. 716 (D. C. N. Y.).

Compare, In *re Grissler*, 13 A. B. R. 510, 136 Fed. 754 (C. C. A. N. Y.), where the court inferentially holds that where the contractor (not the owner) is the bankrupt, the State Court is the proper forum. See owner as adverse claimant, ante, § 1682.

Dispute as to Actual Possession; Also as to Consent.—The determination of the question of fact as to whether there was actually possession or actually consent decided on a conflict of evidence will not be disturbed on review. In *re Kolin*, 13 A. B. R. 531, 134 Fed. 557 (C. C. A. Ills.).

Garnishee on Own Motion Paying Exempt Wages into Court.—A garnishee, on its own petition has been permitted to pay into the bankruptcy court exempt wages, although the State Court had already rendered judgment therefor against the garnishee, and although the judgment creditor did not consent.

In *re McCartney*, 6 A. B. R. 367, 109

Fed. 621 (D. C. Wis.): This case is of doubtful authority inasmuch as the lien in this instance was not void, it being a lien on exempt property over which the bankruptcy court should not assume jurisdiction.

All Claimants Consenting, Except Garnishee.—In *re Kane*, 18 A. B. R. 654, 152 Fed. 587 (D. C. Pa.), quoted, on other points, § 1663.

Possession Acquired by Stipulation for Preservation of Rights without Prejudice Stipulation Not to Be Repudiated.—Where the possession of property which was to be the subject of litigation was acquired by the bankruptcy court from an adverse claimant, upon the faith of a stipulation between it and the receiver, approved by the referee, that its rights should not be prejudiced thereby, the receiver, who succeeded himself as trustee, will not be permitted to repudiate the stipulation, which may have been improvidently made. In *re Newton & Co.*, 18 A. B. R. 567, 153 Fed. 841 (C. C. A. Ark.), affirmed sub nom. *Bryant v. Swofford Bros.*, 22 A. B. R. 111, 214 U. S. 279.

money into the bankruptcy court by consent of all parties, then the bankruptcy court will have complete jurisdiction.

In *re Blake*, 17 A. B. R. 668, 151 Fed. 279 (C. C. A. Mo.): "A court of bankruptcy may acquire by consent of all parties in interest jurisdiction to determine a controversy between the trustee and an adverse claimant concerning an indebtedness of a third party and the lawful power to adjudicate all the claims of the parties thereto and to enforce their rights against each other by decree and execution.

"A court of equity which has acquired jurisdiction of the subject matter and of the parties to a controversy may, and it should, grant complete relief, to the end that litigation over it may cease and a multiplicity of suits may be avoided.

"A trustee in bankruptcy and a county each claimed to recover an indebtedness of a bank for \$16,000, the consideration of which was credits transferred to it by the bankrupts pursuant to an executed agreement to suppress competition in bidding for the use of the county deposits and to divide them. The bank filed a bill in the bankruptcy court wherein it set forth the claims of the county, and the trustee offered to deposit the \$16,000 in court, and prayed to be discharged. The claimants filed answers in which they pleaded their claims and asked to recover the \$16,000. They then made an agreed statement of facts and stipulated that their claims should be determined by the court upon this statement of facts. The court considered the statement, held that the county was entitled to the \$16,000, and ordered the bank to pay it over to the county. The trustee presented a petition for revision. Held, the adjudication in bankruptcy, the controversy between the trustee and the county, and the consent of the parties conferred jurisdiction upon the court to hear the issues upon the agreed statement of facts and to render the judgment, and there was no error in the proceedings nor in the conclusion which had not been waived by the trustee."

Thus, also, an adverse claimant in possession of goods, notes and accounts, may confer jurisdiction on the bankruptcy court by surrendering the same to the receiver; and where the surrender is made to a receiver under the stipulation that it shall be without prejudice to the rights of the parties, the trustee subsequently appointed may not repudiate the stipulation.¹⁷

Bryant v. Swafford Bros., 214 U. S. 279, 22 A. B. R. 111 (affirming *In re Newton & Co.*, 18 A. B. R. 567, 153 Fed. 841): "There seems to be no reason for a nice consideration of the powers of receivers and trustees. When the receiver was appointed he found all the property in dispute in the hands of the dry goods company, to which it had been delivered by the Newtons, as and for the property of the company, and by which it had been received as its own property. When the receiver made his demand for it the return was at first refused. The parties in the controversy then being at arms' length, agreed that if the dry goods company would give up the advantages of possession, and, instead of converting the goods, notes and accounts into cash in its own way and on its own account, permit the receiver to do so, then those goods should be deemed part of those delivered under the contract, and the notes and accounts the proceeds of other goods delivered under the contract. This arrangement was approved by the referee. The trustee has taken the property under it and has never offered to return the property, or any part of it. The property has in large part been sold or otherwise disposed of in the course of the bankruptcy

¹⁷ *In re Newton & Co.* (*Swofford Dry Goods Co. v. Bryant*), 18 A. B. R. 567, 153 Fed. 841 (C. C. A. Ark.).

administration. Under these circumstances we are of opinion that the trustee, the appellant in this case, was bound by the agreement of the receiver, that all the property in dispute should be conclusively deemed that which passed under the original conditional contract, or the proceeds thereof."

But, in case of garnishment, where the garnishee also is an adverse claimant to part of the fund, the consent must also be on his part.¹⁸

Thus, also, an adverse claimant confers jurisdiction by consent when he comes into the bankruptcy court and asks for the surrender of property, or for the declaration of a lien thereon, where the property is in the custody of a trustee in another state.¹⁹

§ 1697. Likewise Debtors Owning Money May Confer Jurisdiction by Consent.—Likewise debtors owing money to the bankrupt, or adverse parties obligated to him otherwise than by reason of property fraudulently or preferentially transferred, may confer jurisdiction on the bankruptcy court by consent.²⁰

§ 1698. What Constitutes Consent.—Whether consent is given or not is a question of fact, to be decided in general in conformity with the usual rules as to consent to jurisdiction over the person. And the findings of the lower court will not be disturbed on a conflict of evidence.²¹

But it appears from some decisions that the consent required by the Bankruptcy Act is intended to be more complete than is sometimes held sufficient to confer jurisdiction elsewhere.²²

Filing a "demurrer" to the jurisdiction and at the same time answering to the merits; and, upon the hearing, urging both grounds, does not show the "consent" meant by the Act;²³ nor does the failure to object to jurisdiction until, by amended petition, a good case is made, constitute such "consent."²⁴

Going to a hearing on the merits, after an overruling of objections to the jurisdiction, of course does not amount to "consent," nor to a waiver of objections.²⁵

Bank v. Title & Trust Co., 14 A. B. R. 106, 198 U. S. 280, reversing 11 A. B. R. 79: "That they then did not abandon their claims did not amount to a waiver

18. In re Kane, 18 A. B. R. 654, 152 Fed. 587 (D. C. Pa.), quoted at § 1663.

19. In re MacDougall, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.).

20. In re White (Froehling v. Amer. Trust & Savings Bank), 24 A. B. R. 197, 177 Fed. 194 (C. C. A. Ill.). Instance held not to show consent, *Louisville Trust Co. v. Comingor*, 7 A. B. R. 421, 184 U. S. 18.

But consent cannot confer jurisdiction where a receiver in bankruptcy attempts to bring an action to recover a money judgment for a preferential payment, for the receiver has no such power. See ante, "Receivers," § 394.

21. In re Kolin, 13 A. B. R. 531, 134 Fed. 557 (C. C. A. Ills.).

22. In re Michie, 8 A. B. R. 734, 116 Fed. 749 (D. C. Mass.); In re Hemby-Hutchinson Pub. Co., 5 A. B. R. 569, 105 Fed. 909 (D. C. Ills.).

23. In re Michie, 8 A. B. R. 734, 116 Fed. 749 (D. C. Mass.).

24. In re Hemby-Hutchinson Co., 5 A. B. R. 569, 105 Fed. 909 (D. C. Ills.).

25. *Louisville Trust Co. v. Comingor*, 7 A. B. R. 421, 184 U. S. 18; In re Bacon, 28 A. B. R. 565, 196 Fed. 986 (D. C. N. Y.).

of their objections or to a consent to an exercise of jurisdiction against which they protested."

And the fact that the defendant did not voluntarily appear, but objected to the power of the court at the hearing, negatives consent.²⁶

The mere proving of one's claim in the bankruptcy proceedings is not a consent to the jurisdiction of the bankruptcy court over property of the bankrupt seized more than four months prior to the bankruptcy by the creditor so proving, where, at any rate, the creditor in his proof insists on his rights by virtue of the seizure; and the State court retains jurisdiction;²⁷ nor does the mere proving of a claim give jurisdiction to render personal judgment against the claimant for the excess of the value of the security retained by him over the amount of his claim.²⁸

On the other hand, answering to the merits without objection is a consent,²⁹ and it has been held that by appearing generally and demurring on grounds going to the merits as well as to the jurisdiction of the court, a defendant waives the objection that the court is without jurisdiction.³⁰ The appearance in the bankruptcy proceedings and, without objection to the jurisdiction, the submission of the questions of ownership or of priority to the referee for adjudication, amount to consent.³¹

The invoking of the affirmative action of the bankruptcy court is certainly a consent;³² as, for instance, a chattel mortgage creditor procuring the bankruptcy court to appoint a receiver and enjoin interference.³³ Acceptance of the benefits of an order of the bankruptcy court is consent.³⁴ And where a third party intervenes in a proceedings brought by the trustee to compel the bankrupt to execute assignments or other papers in aid of the collection of assets, such as assignments of insurance policies or of licenses

26. In re Horgan, 19 A. B. R. 857, 158 Fed. 774 (C. C. A. Mass.).

27. Pickens v. Dent, 9 A. B. R. 47, 187 U. S. 177 (affirming 5 A. B. R. 644, 106 Fed. 653).

28. Fitch v. Richardson, 16 A. B. R. 835, 147 Fed. 196 (C. C. A. Mass.).

29. Ryttenberg v. Schefer, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.): But in this case consent was unnecessary since the fund was already in the hands of the trustee.

Detroit Trust Co. v. Pontiac Sav. Bank, 27 A. B. R. 821, 196 Fed. 29 (C. C. A. Mich.).

30. Sheppard v. Lincoln, 25 A. B. R. 804, 184 Fed. 182 (D. C. N. Y.).

31. In re Steuer, 5 A. B. R. 209, 104 Fed. 976 (D. C. Mass.); Chauncey v. Dyke Bros., 9 A. B. R. 444, 119 Fed. 1 (C. C. A. Ark.), in which case, however, the adverse claimant was not in possession of the res, the bankruptcy court itself having its custody.

In re Connolly, 3 A. B. R. 842, 100 Fed. 620 (D. C. Penn.); In re Emrich,

4 A. B. R. 89, 101 Fed. 231 (D. C. Penn.); McEldowney v. Card, 27 A. B. R. 937, 193 Fed. 475 (C. C. Tenn.); In re Kornit Mfg. Co., 27 A. B. R. 244, 192 Fed. 392 (D. C. N. J.).

In re Durham, 8 A. B. R. 115, 114 Fed. 750 (D. C. Md.), in which case, however, "consent" was not necessary, inasmuch as the property already was in the trustee's custody, and therefore the bankruptcy court was the proper forum. In re Porterfield, 15 A. B. R. 11, 138 Fed. 192 (D. C. W. Va.); In re Rochford, 10 A. B. R. 610, 124 Fed. 182 (C. C. A. S. Dak.).

32. In re Porterfield, 15 A. B. R. 11, 138 Fed. 192 (D. C. W. Va.). Obiter, In re Foundry & Machine Co., 17 A. B. R. 294, 147 Fed. 828 (D. C. Wis.).

33. In re Durham, 8 A. B. R. 115, 114 Fed. 750 (D. C. Md.); In re Had-den-Rodee Co., 13 A. B. R. 604, 135 Fed. 886 (D. C. Wis.).

34. In re Noel, 14 A. B. R. 715, 137 Fed. 694 (D. C. Md.).

or of stock exchange seats, such third parties thereby consent to the jurisdiction;³⁵ although perhaps the res is not strictly in custodia legis.

So, the filing of a petition for reclamation of property which, as assets of the estate, was taken from the person of the bankrupt's agent, confers jurisdiction by consent.³⁶ And where a lienor voluntarily appears before the referee, presents his claim as a secured claim and seeks its allowance, the referee may summarily determine the validity of the lien so asserted.³⁷ An assignee for the benefit of creditors where the assignment has been nullified by the bankruptcy, who invokes the aid of the bankruptcy court, thereby consents to summary jurisdiction,³⁸ even though subject thereto in any event.

Failure to object to the jurisdiction of the federal court over the person of the defendant until the case reaches the reviewing court, constitutes consent and the defendant is too late.³⁹ Failure to object to the jurisdiction of the referee until an adverse decision on the merits, also is a consent.⁴⁰

§ 1699. But Consent Confers Jurisdiction Only in Plenary Actions, unless Property in Custodia Legis.—But this "consent" confers jurisdiction only in cases where the suit is a plenary suit, or where it is a summary proceedings and the property involved is within the possession of the bankruptcy court or subject to its control, in which latter case even the referee may have jurisdiction. The referee would seem not to possess jurisdiction except in the latter case.⁴¹

35. In re Emrich, 4 A. B. R. 89, 101 Fed. 231 (D. C. Penn.).

36. LeMaster v. Spencer, 29 A. B. R. 264, 203 Fed. 210 (C. C. A. Colo.).

37. In re Jackson, etc., Co., 26 A. B. R. 915, 189 Fed. 636 (D. C. Mo.).

38. In re Hays, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio).

39. Boonville Nat'l Bk. v. Blakey, 6 A. B. R. 13, 107 Fed. 891 (C. C. A. Ind.): The fact that by the Amendment of 1903 jurisdiction was conferred in the class of cases herein considered does not affect the decision upon this point in the case of Boonville Nat'l Bk. v. Blakey.

In re Steuer, 5 A. B. R. 209, 104 Fed. 976 (D. C. Mass.); In re Emrich, 4 A. B. R. 89, 101 Fed. 231 (D. C. Penn.).

40. In re Connolly, 3 A. B. R. 842, 100 Fed. 620 (D. C. Penn.); In re Emrich, 4 A. B. R. 89, 101 Fed. 231 (D. C. Penn.). Compare, In re Steuer, 5 A. B. R. 209, 104 Fed. 976 (D. C. Mass.). Also, compare, In re Scherber, 12 A. B. R. 616, 131 Fed. 121 (D. C. Mass.).

41. In re Walsh Bros., 21 A. B. R. 14, 163 Fed. 352 (D. C. Iowa), quoted ante, § 1652; In re Connolly, 3 A. B. R. 842, 100 Fed. 620 (D. C. Penn.), in

which case the bond stood in the place of the property itself, so the case is not contra.

Contra, In re Shults & Marks, 11 A. B. R. 690 (Ref. N. Y.). Also, inferentially, contra, In re Andre, 13 A. B. R. 132, 68 C. C. A. 374 (N. Y.).

Compare, In re Steuer, 5 A. B. R. 209, 104 Fed. 976 (D. C. Mass.): There are some remarks in this case indicating the court held the opinion that jurisdiction to declare a transfer void as a preference could be exercised in any event by the referee upon the transferee's consent to the jurisdiction, but it will be noted the facts do not take the case beyond the rule—the property, to be sure, was not in the actual possession of the bankruptcy court but its representative, the bond for its forthcoming, was in the court's control. Moreover, the consent of the parties actually continued until the case reached the District Judge who had plenary jurisdiction and who in fact treated the proceedings as a plenary suit where the issues had been referred to a referee as special master.

Apparently contra, and apparently to the effect that by consent the referee may order the return of money as a

Compare, inferentially, *Louisville Trust Co. v. Comingor*, 184 U. S. 18, 7 A. B. R. 421: "And the bankruptcy court has no jurisdiction to finally adjudicate the merits of his claims unless by his consent and then only by a plenary suit."

In *re Teschmacher & Mrazay*, 11 A. B. R. 550, 127 Fed. 728 (D. C. Penn.): "The District Court sitting as a court of bankruptcy, may still enquire summarily concerning the ownership of property alleged to belong to the bankrupt, although it be found in the possession or custody of a third person. But if the court should discover that such person is holding the property under a real claim of title or right of possession, and is not merely the alter ego of the bankrupt, it is still the duty of the court to desist from pursuing the summary remedy further, and to remit the contestants to a plenary suit, although the suit, instead of being brought in a State court or a Circuit Court of the United States, may now be brought in the District Court itself, and may there be pursued to a final judgment."

Inferentially and obiter, *Hicks v. Knost*, 2 A. B. R. 153, 158 (D. C. Ohio): "I am inclined to think it has reference not to jurisdiction in bankruptcy courts, but to courts having jurisdiction of the subject matter of the action, but not of the person of the proposed defendant."

Thus, consent of a garnishee and all lienholders, unaccompanied with delivery of the fund into the custody or control of the bankruptcy court, will be insufficient to confer jurisdiction; a fortiori, the consent of merely the lienholders is insufficient.⁴² The consent of merely the garnishee also is insufficient, even where the garnishee pays the money into court, unless such garnishment were void for being a lien created within four months by legal proceedings.

But, at any rate, where the objection is not raised until appeal from the referee's order it comes too late, for the judge has jurisdiction even if the

preference, see obiter, *In re Scherber*, 12 A. B. R. 618, 131 Fed. 121 (D. C. Mass.): "In *re Steuer* (D. C.), 5 Am. B. R. 209, 104 Fed. 976, this court decided that, in proceedings to recover a preference, where the jurisdiction of the referee was not objected to, and where the summary petition contained all the substantial allegations of a bill in equity, the judge, on appeal, from the referee, had jurisdiction to decree the return of the preference, whether the referee originally had jurisdiction of the proceedings or not. See *Bryan v. Bernheimer*, 181 U. S. 188, 5 Am. B. R. 623, where it is implied, if not expressly decided, that consent will give jurisdiction to the referee over a summary petition against an adverse claimant, although, without consent, the court of bankruptcy would be altogether without jurisdiction."

Also, apparently contra, *In re Fowler*, 1 A. B. R. 637 (Ref. Conn.): But in this case it must be noted that the subject matter of the controversy was a patent and that it is doubtful

whether it can be said to have been "held" by the trustee. If the property were actually "held" by the trustee there would have been no reason for refusing jurisdiction to the Bankruptcy Court. Moreover, the point was made that the trustee was not consenting.

Also, apparently contra, *In re O'Brien*, 21 A. B. R. 11 (Ref. Mass.), although in this case it was evident the referee was acting rather as an arbitrator.

Perhaps, impliedly, contra, although it does not definitely appear that the proceedings were before the referee, *In re White* (*Froehling v. Amer. Trust & Savings Bank*), 24 A. B. R. 197, 177 Fed. 194 (C. C. A. Ill.).

The case *In re Blake*, 17 A. B. R. 668 (C. C. A. Mo.), while evidently a case of plenary action, yet on the facts, might have been cognizable before the referee, for there the fund itself was placed in the custody of the Court.

⁴² See § 1663; also, see *In re Kane*, 18 A. B. R. 654, 152 Fed. 587 (D. C. Pa.), quoted at § 1663.

referee does not have it.⁴³

And where the bankrupt's wife has permitted the bankrupt to surrender to the custody of the trustee certain stocks, etc., claimed by her, under an agreement that her rights of ownership shall be determined, but without objection to the jurisdiction, she has consented.⁴⁴

And where the property once was in the custody of the bankruptcy court, but has been erroneously taken therefrom, the referee has jurisdiction summarily to order its return, under the doctrine of § 1800, post.

Obiter, In re Tarbox, 26 A. B. R. 432, 185 Fed. 985 (D. C. Mass.): "If it be said that Mrs. Piper might have waived all objections to the referee's jurisdiction, had she been summoned, it is doubtful whether consent can give jurisdiction in summary proceedings."

§ 1700. No Jurisdiction by Consent Where No Custody and Neither Litigant Party to Bankruptcy Proceedings.—But, as noted ante, § 1693, third parties cannot by consent confer jurisdiction on the bankruptcy court when neither that court has custody of any property involved nor neither litigant was a party to the proceedings in bankruptcy. Thus, the bankruptcy court will not entertain a bill by a third party against a purchaser from the trustee where the dispute is wholly between such third party and purchaser.⁴⁵

Henrie v. Henderson, 16 A. B. R. 621, 145 Fed. 316 (C. C. A. W. Va., reversing In re Henderson, 15 A. B. R. 760): "Even though it appears that the petitioner did not object to the Federal Court taking jurisdiction of this case, this court would of its own motion refuse to entertain jurisdiction of the parties if it does not affirmatively appear in the record that the court below had jurisdiction. * * *

"This is not a case in bankruptcy in any sense of the word. It is not contended that either the plaintiff or defendant were parties to the proceeding before the referee in bankruptcy."

But, of course this proposition is to be taken with the qualification of § 1800, that property once in the custody of the bankruptcy court but wrongfully taken therefrom, may be summarily ordered returned.

§ 1701. Trustee May Not Object, if Adverse Claimant Consents.—If the adverse claimant himself consents or voluntarily invokes the affirmative action of the bankruptcy court, the trustee will not be heard to object to the jurisdiction.⁴⁶

§ 1702. Thus, Not to Plenary Suit in Bankruptcy Court by Adverse Claimant in Possession.—Thus, an adverse claimant in possession

⁴³ In re Steuer, 5 A. B. R. 209, 104 Fed. 976 (D. C. Mass.); In re Scherber, 12 A. B. R. 619, 131 Fed. 121 (D. C. Mass.).

⁴⁴ In re Bacon, 20 A. B. R. 107, 159 Fed. 424 (C. C. A. N. Y.).

⁴⁵ See ante, § 1693.

⁴⁶ In re Hadden-Rodee Co., 13 A. B. R. 604, 135 Fed. 886 (D. C. Wis.). Contra, In re Fowler, 1 A. B. R. 637 (Ref. Conn.).

of the res may institute and maintain in the United States District Court in bankruptcy a plenary petition to enjoin the trustee from interfering with his possession or beclouding his title.

Warehousing Co v. Hand, 16 A. B. R. 56, 143 Fed. 32 (C. C. A. Wis., affirmed in 206 U. S. 415, 19 A. B. R. 291): "The pleadings filed by the appellants in the District Court were in substance bills of equity to establish and enforce their liens and rights of possession, and to enjoin the appellees from beclouding their rights and disturbing their possession. The District Court, on the initiative of the appellants, had complete jurisdiction to determine these questions in a plenary suit, which was an independent controversy between adverse claimants and the trustees, and was not a part of the proceedings in the administration of the estate."

§ 1703. No Indirect Review by Suing Trustee in United States District Court, Where Litigants Dissatisfied in Bankruptcy Proceedings.—But dissatisfied litigants in the bankruptcy proceedings may not obtain indirect review by suing the trustee in the United States District Court. Thus, a suit to enjoin the trustee from paying dividends will not be entertained by the United States District Court.⁴⁷

§ 1704. After "Consent" Too Late to Retract.—After consent to the jurisdiction it is too late to retract and prefer jurisdictional defenses.⁴⁸

SUBDIVISION "B."

ANCILLARY BANKRUPTCY PROCEEDINGS AND PROPERTY LOCATED IN OTHER DISTRICTS; ACTIONS OUTSIDE DISTRICT WHERE THE BANKRUPTCY PROCEEDINGS PENDING.

§ 1705. "Ancillary" Bankruptcy Proceedings Maintainable.—"Ancillary" bankruptcy proceedings in another district are maintainable.⁴⁹

47. *Hatch v. Curtin*, 16 A. B. R. 629, 146 Fed. 200 (C. C. A. Mass.). See ante, § 1693.

48. *Obiter*, In re *Durham*, 8 A. B. R. 115, 114 Fed. 750 (D. C. Md.), which case is obiter for the reason that consent was not necessary to confer jurisdiction, the property being in the possession of the bankruptcy court.

In re *Kolin*, 13 A. B. R. 533, 134 Fed. 557 (C. C. A. Ills.); In re *Rochford*, 10 A. B. R. 610, 124 Fed. 182 (C. C. A. S. Dak.); In re *Bacon*, 20 A. B. R. 107, 159 Fed. 424 (C. C. A. N. Y.); *Detroit Trust Co. v. Pontiac Sav. Bank*, 27 A. B. R. 821, 196 Fed. 29 (C. C. A. Mich.).

49. Bankr. Act, § 2, as amended in 1910: "That the courts of bankruptcy, as hereinbefore defined, * * * are hereby invested, within their respective territorial limits as now established * * * with such jurisdiction at law and in equity as will enable them

to * * * (20) exercise ancillary jurisdiction over persons or property within their respective territorial limits in aid of a receiver or trustee appointed in any bankruptcy proceedings pending in any other court of bankruptcy." In re *Madson Steel Co.*, 216 U. S. 115, 23 A. B. R. 614; (1867) *Lathrop v. Drake*, 91 U. S. 516; (1867) *Sherman v. Bingham*, Fed. Cases, No. 12,762, 7 N. B. Reg. 490; (1867) In re *Tift*, Fed. Cases, No. 14,034, 19 N. B. Reg. 201; (1867) *McGehee v. Hentz*, Fed. Cases, No. 8,794; In re *Peiser*, 7 A. B. R. 690, 115 Fed. 199 (D. C. Pa.); In re *Sutter*, 11 A. B. R. 632, 131 Fed. 654 (D. C. N. Y.); In re *Benedict*, 15 A. B. R. 232, 140 Fed. 55 (D. C. Wis.). Apparently obiter, In re *Owings*, 15 A. B. R. 475, 140 Fed. 739 (D. C. N. C.); In re *Lipman*, 29 A. B. R. 139, 201 Fed. 169 (D. C. N. J.); In re *Musica & Son*, 30 A. B. R. 555, 205 Fed. 413 (D. C. La.);

Babbitt, Trustee, v. Dutcher, 216 U. S. 102, 23 A. B. R. 519: "On the authority of these decisions it must be, and is, conceded that under the Bankruptcy Acts of 1841 and 1867 ancillary jurisdiction, both in summary proceedings and in plenary suits, existed in all District Courts within their respective districts; and the question really is whether the provisions of the Act of 1898 are to the contrary, or, as appellee's counsel puts it, show an intention on the part of Congress to restrict such jurisdiction so as to cut off the inferences drawn from the language of the earlier acts. But neither the Act of 1867 nor the Act of 1898 expressly confers or expressly negatives ancillary jurisdiction in courts other than the court of adjudication. The provisions as to summary jurisdiction in the two acts are substantially identical, and, it appears to us, should receive the same construction."

Acme Harvester Co. v. Beekman Co., 222 U. S. 300, 27 A. B. R. 262: "As to the injunction, we are of the opinion that there was no power in the District Court to issue an ex parte injunction, without notice or service of process, attempting to restrain the Beekman Lumber Company from suing in a State outside the jurisdiction of the District Court. Such proceeding could only have binding force upon the Lumber Company if jurisdiction were obtained over it by proceedings in a court having jurisdiction, and upon service of process upon such creditor.

"Whether ancillary proceedings could be had in a District Court in aid of the jurisdiction of an original court of bankruptcy was a subject of much discussion and divers decisions in the Federal courts. In *Babbitt, Trustee, v. Dutcher*, 216 U. S. 102, 23 A. B. R. 519, and *Elkus, petitioner, In the Matter of the Madson Steel Company, Bankrupt*, 216 U. S. 115, 23 Am. B. R. 614, the matter came before this court, and it was there determined that there was ancillary jurisdiction in the courts of bankruptcy, in aid of the original jurisdiction in the bankruptcy court, to make orders and issue processes summarily in aid of the original jurisdiction. In the opinion in *Babbitt v. Dutcher* it was pointed out by Mr. Chief Justice Fuller, speaking for the court, that the jurisdiction of the bankruptcy courts under the act of 1898 was limited to their respective territorial limits, and was in substance the same as that provided by the act of 1867, giving such courts jurisdiction in their respective districts in matters of proceedings in bankruptcy. The necessary deduction from these cases is to deny to the District Courts jurisdiction such as was sought to be asserted in this case by the issuing of an injunction against one not a party to the proceeding, and which undertook to have effect in the distant jurisdiction outside the territorial jurisdiction of the District Court. Under the act of 1898, as expounded in the two cases in 216 U. S. (23 Am. B. R.) supra, the injunction might have been sought in the District Court

compare, instance, *In re United Buton Co.*, 12 A. B. R. 761 (D. C. N. Y.); *In re Schrom*, 3 A. B. R. 352, 97 Fed. 760 (D. C. Iowa); *In re Nelson Co.*, 18 A. B. R. 66, 149 Fed. 590 (D. C. N. Y.); [1867] *In re Richardson, Fed. Cases, No. 11,774*; (1867) *Marckson v. Heaney, Fed. Cases, No. 9,098*, 1 Dill. 497. Contra (before decision of United States Supreme Court in *Babbitt v. Dutcher*, supra), *In re Van Hartz*, 15 A. B. R. 747, 142 Fed. 726 (C. C. A. N. Y.); also, contra (before the decision of *Babbitt v. Dutcher*, supra), *In re Granite City Bank*, 14 A. B. R. 404, 137 Fed. 818 (C. C. A. Iowa); also, contra (before decision of *Babbitt v. Dutcher*, supra), *In re Williams*, 10 A. B. R. 538, 123 Fed.

321 (D. C. Tenn.); contra (before *Babbitt v. Dutcher*, supra), *Foundry Co. v. Foundry Co.*, 10 A. B. R. 624, 124 Fed. 403 (D. C. Tenn.); contra, (before decision of *Babbitt v. Dutcher*) *In re Tybo Mining & Reduction Co.*, 13 A. B. R. 62, 132 Fed. 699 (D. C. Nevada); also, contra (before the Supreme Court's decision in *Babbitt v. Dutcher*, supra), *In re Williams*, 9 A. B. R. 744, 120 Fed. 38 (D. C. Ark.); also contra, *In re Dunseath & Son Co.*, 22 A. B. R. 75, 21 A. B. R. 742, 168 Fed. 973 (D. C. Pa.); also contra, *Hull v. Burr*, 18 A. B. R. 541, 153 Fed. 945 (C. C. A. Fla.), also contra (before decision of *Babbitt v. Dutcher*) *In re Dempster*, 22 A. B. R. 751, 172 Fed. 353 (C. C. A. Mo.).

of the United States in the District in Missouri where personal service could have been made upon Beekman Lumber Company. Since the decision in the cases just referred to, Congress has passed the act of June 23, 1910, amending the bankruptcy law, specifically giving ancillary jurisdiction over persons and property within their respective territorial limits to the District Courts of the United States in aid of the receiver or trustee appointed in a bankruptcy proceeding pending in another court of bankruptcy. Statutes of the U. S. of 1909 and 1910, part 1, page 838."

Fidelity Trust Co. v. Gaskell, 28 A. B. R. 4, 195 Fed. 865 (C. C. A. Mo.): "Attention is called to the fact that by the Act of June 25, 1910, 'ancillary jurisdiction over persons or property within their respective territorial limits' is granted to the District Courts 'in aid of a receiver or trustee appointed in any bankruptcy proceedings pending in any other court of bankruptcy,' and it is contended that the true construction of this grant is that it makes the District Court the agent, the mere hand of the receiver or trustee appointed by the court of primary jurisdiction, bound to seize, convert into money, pay over to him and send to that court the proceeds of any property in its territorial jurisdiction which he may point out as the property of the bankrupt, without judicial power or duty to inquire or to decide, whether the property it takes and sends forth beyond its jurisdiction is that of the bankrupt or of a stranger what legal or equitable liens are held upon it by the citizens of its district, what the expenses of its officers are, or what their compensation shall be and without power to pay them out of the proceeds of the property it seizes and sells. If such had been the purpose of Congress it would undoubtedly have conferred this power on the receiver or trustee of the court of primary jurisdiction directly. It was probably because the Congress was unwilling to entrust the power to such an officer and desired to invoke the judicial power and discretion of a court of equity to inquire and decide what property ought to be seized and sold and what proceeds ought to be sent to the court of primary jurisdiction as the property of the bankrupt's estate that it conferred this ancillary jurisdiction upon the District Courts within their respective territorial limits. Under it these courts must appoint their own receivers, must guard them against wrongful action and consequent liability and must direct the course they shall pursue. Conscience, good faith and reasonable diligence alone move courts of equity to action. They may not be divested of their judicial functions and made mere cat's paws to do the will of private parties or public officers, even by legislative action, much less by mere construction. Moreover, it would be unjust, unwise and detrimental to the administration of justice to establish the rule that courts of ancillary jurisdiction under the bankruptcy law are without judicial power or duty to hear and decide whether the property they take is that of the bankrupt or of strangers, that they must seize and send to the court of original jurisdiction the proceeds of whatever property the receiver or trustee appointed by that court claims as the property of the bankrupt and that adverse claimants of title to or liens upon it, and even its own officers, have no remedy for the enforcement of their claims but to follow the proceeds to other jurisdiction or to sue the receiver. Nor is this the natural or national interpretation of the Act of Congress or of the decisions of the Supreme Court. That Act and those decisions are that the District Courts sitting in bankruptcy, and consequently in equity, have ancillary jurisdiction in bankruptcy proceedings pending in other districts. Ancillary jurisdiction is a term which has a plain and well-known meaning in the equity jurisprudence of the United States, a meaning fixed by settled practice and adjudged by the uniform current of the decisions of the courts of the United States. As neither the court nor the Congress modified or limited the term the unavoidable presumption is that they used it, and intended to use it, in its recognized

legal significance. In that significance ancillary jurisdiction includes the power to hear and adjudge, at the request of interveners, their claims to title to, or legal or equitable lien upon, the property it takes, or holds in its legal custody, by virtue of that jurisdiction and to send the proceeds to the court of original jurisdiction, or to apply it to the discharge of the claims of the interveners in accord with its decision."

§ 1705¼. Issuing and Enforcing Process Outside District.—

Whilst the bankruptcy court in possession of a res may issue citation or other process and have it served upon parties in another district to appear and show what interest they have in such res and why contemplated action in relation thereto should not be taken, yet it cannot issue nor enforce summary orders nor process in another district.

Staunton v. Wooden, 24 A. B. R. 736, 179 Fed. 61 (C. C. A. Calif.): "In the present case the court made a summary order, directed against a resident of another State, ordering him to surrender property in that State to the trustee. It may be conceded that the court in which the petition in bankruptcy is filed has plenary jurisdiction in bankruptcy, coextensive with the United States, to order and control the disposition of the bankrupt's estate, and is vested with jurisdiction to determine all liens thereon and all interests affecting it. *Thomas v. Woods* (C. C. A., 8th Cir.), 23 Am. B. R. 132, 173 Fed. 585, 97 C. C. A. 535; *In re Dempster* (C. C. A., 8th Cir.), 22 Am. B. R. 751, 172 Fed. 353, 97 C. C. A. 51; *In re Muncie Pulp Co.* (C. C. A., 2d Cir.), 18 Am. B. R. 56, 151 Fed. 732, 81 C. C. A. 116; *Guardian Trust Co. v. Kansas City Southern Ry. Co.*, 171 Fed. 43, 96 C. C. A. 285; *In re Granite City Bank* (C. C. A., 8th Cir.), 14 Am. B. R. 404, 137 Fed. 818, 70 C. C. A. 316. But this is not to say that the court of bankruptcy may issue its process to run into another district. It is one thing to issue citation to persons in another jurisdiction to appear before the court of bankruptcy in a proceeding which, in its exclusive jurisdiction, it is authorized to institute with a view to determining liens or rights of property wherever situate; but it is quite another thing to issue process to be enforced in another jurisdiction.

"By whom is the summary order in this case to be executed, and in what manner is obedience to it to be enforced? There is no express provision in the Bankruptcy Act, or in any statute, indicating the intention of Congress to confer such power. In *Toland v. Sprague*, 12 Pet. 328, 9 L. Ed. 1093, it was said: 'Whatever may be the extent of their jurisdiction over the subject-matter of suits, in respect to persons and property, it can only be exercised within the limits of the district. Congress might have authorized civil process from any Circuit Court to have run into any State of the Union. It has not done so.' The Bankruptcy Act of 1867 (Act March 2, 1867, c. 176, 14 Stat. 517) limited the jurisdiction of courts of bankruptcy to 'their respective districts.' The present act invests them with jurisdiction 'within their respective territorial limits as now established, or as they may be hereafter changed;' and it has been held that a court of bankruptcy may not extend its process beyond the territorial limits of the district within which its ordinary jurisdiction may be exercised. In *re Waukesha Water Co.* (D. C. Wis.), 8 Am. B. R. 715, 116 Fed. 1009; *In re Alpin & Lake Cotton Co.* (D. C. Ark.), 12 Am. B. R. 653, 161 Fed. 886. In view of these considerations, and the authorities, we are of the opinion that the District Court was not possessed of jurisdiction to make and enforce the summary order."

[1867] *Lathrop v. Drake*, 91 U. S. 516: "When the Act says they shall have jurisdiction in their respective districts, it means that the jurisdiction is to be exercised in their respective districts."

Such citations or other process must issue out of the court exercising ancillary jurisdiction within the district wherein they are to be served.⁵⁰

§ 1706. But May Marshal Liens and Sell Personal Property in Actual Custody Though in Another State.—But the bankruptcy court, including the referee, has the power to marshal liens and sell free therefrom personal property in the actual possession of its trustee, receiver, bankrupt, or agent of either, although the property and lienor are located in another state.⁵¹

In re Granite City Bank, 14 A. B. R. 404, 137 Fed. 818 (C. C. A. Iowa, affirming In re Wilka, 12 A. B. R. 727, 131 Fed. 1004): "Counsel for the bank seem strangely affected with notions about State lines under the Bankrupt Act. They challenge the right to reach the bank in South Dakota by notice sent out by the referee in Iowa, and the right of the court in bankruptcy in Iowa to draw the bank from its residence in South Dakota to determine its rights as a preferred mortgagee. Under the scheme of the Bankrupt Act, the District Court of the domicile of the bankrupt takes exclusive jurisdiction of the bankrupt and his property, wherever situated, to administer it and distribute the proceeds *pari passu* among the creditors according to their respective rights and priorities. Only one court—the court making the adjudication—collects, marshals, administers, determines priorities of the parties, and directs the distribution of the assets. There are no such things in bankruptcy proceedings as courts of primary and ancillary jurisdiction. The court in this instance acquired jurisdiction as to the Granite City Bank by giving the notice prescribed by § 58 of the Act, which in this case was supplemented by notice served personally on the president of the bank where the bank was located. The bank could have appeared and contested at its pleasure the propriety of the referee ordering the sale of the property free from all liens, and the District Court of Iowa, and it alone, could pass upon the validity of the bank's claim to the proceeds of the sale of the property. In re Kellogg, 10 Am. B. R. 7, 121 Fed. 333, 57 C. C. A. 547. The trustee was authorized to sell the property on the premises in South Dakota, or drive it away, as the court might direct. The Granite City Bank could not replevin it from the trustee. *White v. Schloerb*, 178 U. S. 542, 4 Am. B. R. 178."

Although the decision of the Supreme Court in *Babbitt v. Dutcher* [quoted at § 1705] holds ancillary jurisdiction to exist, and the Amendment of 1910 expressly confers ancillary jurisdiction, yet such right of the court of original jurisdiction, to marshal liens and to sell property in actual custody, though in another State, doubtless still exists.

^{50.} In re Brocton Ideal Shoe Co., 29 A. B. R. 76, 200 Fed. 745 (C. C. A. N. Y.).

^{51.} In re Wilka, 12 A. B. R. 727, 131 Fed. 1004 (D. C. Iowa, affirmed sub nom. In re Granite City Bank, 14 A. B. R. 404, 137 Fed. 818, C. C. A. Iowa).

But compare, In re Owings, 15 A. B. R. 476, 140 Fed. 759 (D. C. N. Car.), as to setting apart homestead in property located in another State.

Setting Apart Dower in Another State.—It has been held, however, that the court of bankruptcy wherein the proceedings are pending has jurisdiction to set apart dower and determine rights in land in the custody of the trustee or bankrupt in another State. *Hurley v. Devlin*, 18 A. B. R. 627, 151 Fed. 919 (D. C. Kan.), quoted at § 1706½; *Thomas v. Woods*, 23 A. B. R. 132, 173 Fed. 585 (C. C. A. Kans.), quoted at § 1706½.

§ 1706½. **How as to Real Estate in Another State.**—But it is doubtful whether the bankruptcy court wherein the adjudication of bankruptcy was had may marshal liens upon, or determine rights in, real estate located in another State. Nevertheless, it has been held that dower rights may be so determined where the trustee has actual custody of the real estate in the other State.

Hurley v. Devlin, 18 A. B. R. 627, 151 Fed. 919 (D. C. Kan.): "From the facts as stated, and from the very nature of the jurisdiction possessed by this court in bankruptcy proceedings, I am of the opinion the jurisdiction and power to determine the rights of the widow to dower in the property of her bankrupt husband, deceased during the pendency of the proceedings under the Bankruptcy Act, is exclusively in this court; that the State courts of Illinois and Missouri do not possess such jurisdiction; that the ancillary bill presented to this court by the trustees, and the order of this court made thereon restraining the resident widow from further prosecuting such suits brought by her in the State courts where the property is located, were rightfully filed and made, and that the motion to set aside such order must be overruled and denied." Quoted further at § 1166½.

And it seems that real estate located in another district or its proceeds may be in the custody of the bankruptcy court, so that marshaling of liens thereon may be had in the original bankruptcy proceedings, without the institution of ancillary proceedings.⁵²

Thomas v. Woods, 23 A. B. R. 132, 173 Fed. 585 (C. C. A. Kans.): "The objection of the appellant that the trial court was without jurisdiction of the property, because it was not situated in the District of Kansas has no merit. Upon the filing of a petition in bankruptcy, all property held by or for the bankrupt is brought within the custody of the court of bankruptcy, and, upon adjudication, that court is vested with jurisdiction to determine all liens and interests affecting it. This jurisdiction is co-extensive with the United States."

§ 1707. Property in Other States Not in Actual Custody, to Be Protected Only by Independent Suit or Ancillary Proceedings.—

Property not in the actual custody of the receiver or trustee in bankruptcy, located in other districts than the one where the bankruptcy proceedings are pending, can be protected only by separate suits brought within such districts, or by ancillary proceedings therein instituted;⁵³ and neither summary nor plenary proceedings can be maintained in the original bankruptcy case to reach such property in other districts.⁵⁴

52. *In re MacDougall*, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.). *In re Muncie Pulp Co.*, 8 A. B. R. 56, 151 Fed. 732 (C. C. A. N. Y.).

53. *In re Peiser*, 7 A. B. R. 690, 115 Fed. 199.

54. Compare, before Supreme Court decision in *Babbitt v. Dutcher*, also be-

fore Amendment of 1910, *Ross-Meehan Fdy. Co. v. Southern Car & Fdy. Co.*, 10 A. B. R. 624, 124 Fed. 403 (D. C. Tenn.).

Setting Apart Homestead in Another State.—Where a person having a domicile in one state is adjudicated a bankrupt therein, it has been held that the

In *re Heintz*, 29 A. B. R. 19, 201 Fed. 388 (C. C. A. Ohio): "Congress, by express enactment, has vested in the several courts of bankruptcy, 'within their respective territorial limits,' full and complete power and authority to try and determine bankruptcy controversies and specifically to 'cause the estates of bankrupts to be collected, reduced to money and distributed, and determine controversies in relation thereto.' The jurisdiction thus defined and conferred is exclusive within the territorial limits of each court and confined to those limits. While a summary proceeding to collect property belonging to the estate of a bankrupt which is in the possession of a stranger who resides outside of the territorial limits of the court of the original adjudication is ancillary in character, nevertheless it presents a completely distinct and separable controversy, and, therefore, one which must be determined by the court within whose jurisdiction the property is located and the respondent resides. Any other rule would result in unnecessary confusion of authority and would do violence to the plain provisions of the Bankruptcy Act."

In *re Rathfon Bros.*, 29 A. B. R. 22, 200 Fed. 108 (D. C. Mich.): "Upon reason and principle, as well as authority, a trustee in bankruptcy, in a proceeding of this kind, ought to be compelled to resort to the court within whose territorial jurisdiction respondent resides and the property sought to be covered is located. By so doing both confusion of authority and circuitry of action will be avoided, for it must be conceded that the court of the original bankruptcy proceedings has no authority to compel the performance of or to enforce obedience to its orders beyond its territorial limits, and in those regards the aid of another court must be asked and procured. While the proceedings in another court is ancillary in character, it presents a completely distinct and separable controversy, and Congress, by express enactment, has vested in the several courts of bankruptcy, 'within their respective territorial limits,' full and complete power and authority to try and determine all bankruptcy controversies, whether arising in original or ancillary proceedings."

In no event may the bankruptcy court in the original case maintain proceedings against a person in possession of property in another district to inquire whether he is a bona fide "adverse claimant," such that summary process may be proper.⁵⁶

§ 1708. Bankruptcy Receiver's Power in Another District Before Adjudication.—Before adjudication the bankruptcy receiver may not go into another State and institute proceedings there for the recovery of property.⁵⁷

In *re Dunseath & Son Co.*, 22 A. B. R. 75, 168 Fed. 973 (D. C. Pa.): "The weight of authority is that the receiver appointed by the District Court of

court of bankruptcy has no jurisdiction to set apart to him a homestead in lands located in another state. *Obiter*, In *re Owings*, 15 A. B. R. 472, 140 Fed. 739 (D. C. N. Car.). Especially would complications arise if the homestead lands of the two states were different and the homestead were set apart in accordance with the law of

the domicile, as required by § 6.

In *re Boston-Cerrellos Corporation*, 30 A. B. R. 739, 206 Fed. 794 (D. C. N. Mex.).

56. Inferentially, In *re Waukesha Water Co.*, 8 A. B. R. 715, 116 Fed. 1009 (D. C. Wis.).

57. See ante, § 395. In *re Schrom*, 3 A. B. R. 352, 97 Fed. 769 (D. C. Iowa).

one district cannot maintain an action in the District Court of another district to recover assets in the hands of strangers. The extraterritorial power of a receiver was carefully considered in the case of *Clark v. Booth*, 17 How. 327, and it was there decided that the receiver possessed no such power. This case was referred to in the case of *Hale v. Allison*, 188 U. S. 56, where Mr. Justice Peckham in commenting on the case of *Clark v. Booth*, said: 'We do not think anything has been said or decided in this court which destroys or limits the controlling authority of that case.' In our own circuit Judge McPherson, sitting in the Eastern district of Pennsylvania, in the case of *In re National Mercantile Agency*, 128 Fed. 639, 12 Am. B. R. 189 (D. C.), decided that a receiver in bankruptcy under an order to collect and take possession of all the assets of an alleged bankrupt is not authorized to bring suits in a district other than the one in which he was appointed, and shows that this position is sustained by the highest authority. We must therefore conclude that the receiver in the case at bar cannot maintain a suit in this district. Under the prevailing authorities he certainly cannot by a summary proceeding such as is brought in this case either restrain the state officers or recover the assets of the bankrupts from the hands of strangers."

The proper practice is for creditors, during the meanwhile, themselves to institute the ordinary remedies of creditors, or for ancillary proceedings to be instituted in aid of the receiver.⁵⁸

§ 1709. After Adjudication, Trustee (and Perhaps Also Receiver) May Institute Proceedings in Another District.—After adjudication the trustee and perhaps the receiver, appointed in one district, however, may go into another district and institute replevin suits or fraudulent transfer suits;⁵⁹ or any other actions necessary to protect the property there;⁶⁰ but a receiver may not do so,⁶¹ unless he be authorized by order of court, for he has only such power as the court that appoints him chooses to give; and, unless he is authorized to leave the court of original jurisdiction and sue elsewhere, he is not competent to bring such suit.⁶² And apparently it has been held in some cases that the receiver may not do so even when ex-

58. *In re Schrom*, 3 A. B. R. 352, 97 Fed. 760 (D. C. Iowa); *Babbitt, trustee, v. Dutcher*, 23 A. B. R. 519, 216 U. S. 102; *In re Madson Steele Co.*, 216 U. S. 115, 23 A. B. R. 614; *Bankr. Act*, amended 1910, § 2 (20).

59. *Lawrence v. Lowrie*, 13 A. B. R. 297, 133 Fed. 995 (D. C. Pa.); *Teague v. Anderson Hdw. Co.*, 20 A. B. R. 424, 161 Fed. 165 (D. C. Ga.); impliedly, but obiter, *Hull v. Burr*, 18 A. B. R. 541, 153 Fed. 945 (C. C. A. Fla.).

60. Compare, *In re Peiser*, 7 A. B. R. 690, 115 Fed. 199 (D. C. Pa.); compare, obiter, *In re Williams*, 10 A. B. R. 541, 120 Fed. 321 (D. C. Tenn.).

61. *In re Benedict*, 15 A. B. R. 232, 140 Fed. 55 (D. C. Wis.).

62. *In re National Mercantile Agency*, 12 A. B. R. 189, 128 Fed. 639 (D. C. Penn.): In this case the court held that a receiver in bankruptcy, under an order empowering him to proceed forthwith to collect and take possession of all the assets of the alleged bankrupt, was not authorized to bring suits in a district other than the one in which he was appointed, the court saying: "As is well known a receiver has such power only as the court, that appoints him chooses to give, and unless he is authorized to leave the court of original jurisdiction and sue elsewhere, he is not competent to bring such a suit." Compare, analogously, *Boonville Nat'l Bk. v. Blakey*, 6 A. B. R. 13, 107 Fed. 891 (C. C. A. Ind.).

pressly authorized.⁶³

The trustee, however, need not obtain special authority to go into another district to institute legal proceedings.

Obiter, *In re Nat'l Mercantile Agency*, 12 A. B. R. 189, 128 Fed. 639 (D. C. Pa.): "It is manifest, therefore, that the receiver was without power to institute this proceeding, and for this reason the petition must be dismissed. No injury, however, is likely to be done to the bankrupt estate, for, as I am informed, a trustee has since been appointed and he has ample power to bring an action in the proper form to recover whatsoever assets of the bankrupt may be found in the possession of other persons."

Of course, ancillary proceedings may be instituted in another district in aid of either the receiver or trustee.

§ 1709½. Scope of Ancillary Proceedings.—Any District Court in bankruptcy in the exercise of ancillary jurisdiction in aid of another bankruptcy court may grant injunctions, stay proceedings and enforce compositions.⁶⁴

Fidelity Trust Co. v. Gaskell, 28 A. B. R. 4, 195 Fed. 865 (C. C. A. Mo.): "A court exercising ancillary jurisdiction acts independently of the court of primary jurisdiction, or of its officers and for itself. It appoints its own receiver, generally the same person appointed receiver by the court of primary jurisdiction, but in the seizure, management, sale and distribution of the property seized within the territorial limits of its district, of which it takes the legal custody, this receiver is, and must be, governed by its orders exclusively."

It may also order the summary delivery of property and documents,⁶⁵ and enforce the examination of bankrupts and witnesses,⁶⁷ and marshal liens,⁶⁸ the same as the original bankruptcy court could have done had the parties been within the jurisdiction.

It may order the treasurer, or other officer, of a bankrupt corporation, to file schedules in bankruptcy, especially where such officer is the person who knows most about the bankrupt's affairs.⁶⁹

SUBDIVISION "C."

OTHER ACTIONS THAN THOSE TO SET ASIDE FRAUDULENT AND PREFERENTIAL TRANSFERS.

§ 1710. Other Actions Maintainable by Trustee.—The trustee of

^{63.} Compare, *Booth v. Clark*, 17 How. 327; *Hale v. Allison*, 188 U. S. 56; *Great Western Mineral & Mfg. Co. v. Harris*, 198 U. S. 561.

^{64.} *In re Tifft*, 19 Nat. Bankr. Reg. 201.

^{65.} *Babbitt v. Dutcher*, 23 A. B. R. 519, 216 U. S. 102; *In re Madson Steel Co.*, 23 A. B. R. 614, 216 U. S. 115.

^{67.} *In re Robinson*, 24 A. B. R. 617, 179 Fed. 724 (D. C. Minn.), quoted at § 1572½; [1867] *In re Tifft*, 19 Nat. Bankr. Reg. 201. Compare post, § 1867.

^{68.} [1867] *In re Tifft*, 19 Nat. Bankr. Reg. 201.

^{69.} *In re Brockton Ideal Shoe Co.*, 29 A. B. R. 76, 200 Fed. 745 (C. C. A. N. Y.).

course may maintain other suits than those brought to recover property fraudulently or preferentially transferred.⁷⁰ •

Thus he may maintain a stockholder's bill to vacate a sale of the assets of a corporation whereof the bankrupt was a member.⁷¹

§ 1711. Whether May Maintain Partition Proceedings.—But it is doubtful whether the trustee may institute partition proceedings, although to realize upon a bankrupt parcener's share.⁷²

Nevertheless, the trustee of a bankrupt heir may file exceptions to the account of the decedent's administrator and contest the same, and so even where the bankrupt is himself the administrator.⁷⁴

Lindsay, as Trustee, *v. Runkle*, 82 Ohio State, 325, 24 A. B. R. 612: "Is he a tenant in common, or is he but the trustee of a tenant in common? He is invested with the title of the bankrupt, not as a purchaser, or under other form of contract, but solely by operation of law and for a special purpose, that he may convert the estate into money with which to pay the debts of the bankrupt. He may, in the bankruptcy proceedings, and according to the law on that subject, sell the undivided interest of the bankrupt in the lands, and convey such interest to the purchaser, who may thus become a tenant in common with the owners of the other interests, and that path appears to be free from doubt or obstruction.

"But what confronts the trustee as he asks partition in the state court The suit must be entertained and conducted under the laws of the State. What would the trustee do or say, in case one or more of the tenants in common should answer and charge that the bankrupt tenant in common had received and enjoyed the rents and profits of the estate for years, and ask an accounting for the same? * * *

"The sale in the partition case is governed by prescribed rules which, as we see by comparison, are in plain conflict with the provisions for sale in the bankrupt proceeding, and the trustee seems insistent in promoting and maintaining that conflict. We know of no method of blending these jurisdictions in order to have partition made that will be just and equitable to the widow and all the tenants in common as their rights may appear.

"It is not our duty to entertain the suit of the trustee when it is inevitable that a conflict of jurisdiction will arise between the State and Federal courts. The trustee may sell the estate of the bankrupt without partition, as before observed, with results less harmful than a complication of questions and interests likely to follow such an action for partition."

70. See post, §§ 1724, 1729, et seq.

71. *Greenhall v. Carnegie Trust Co.*, 25 A. B. R. 300, 180 Fed. 812 (D. C. N. Y.).

72. Holding that he may not maintain

partition. *Hobbs v. Frazier*, 56 Fla. 796, 21 L. R. A. (N. S.) 105, 22 A. B. R. 684.

74. *In re Clute*, 2 A. B. R. 376 (Super. Court San Francisco, Calif.).

DIVISION 3.

WHO MAY BRING PLenary SUITS AGAINST ADVERSE CLAIMANTS.

§ 1712. **Who May Bring Plenary Suits against "Adverse Claimants."**—Before (but not after) the appointment and qualification of the trustee creditors may institute the ordinary suits for the sequestration or recovery of assets to which they would have been entitled had there been no bankruptcy, subject to the control, by restraining orders, of the bankruptcy court; and upon adjudication and the appointment of a trustee, the trustee may be made a party therein, and the lien of the legal proceedings be preserved for the benefit of the estate.⁷⁵

As we have seen (ante, § 399, et seq.), creditors, until adjudication, are entitled to make use of all the usual and ordinary remedies of creditors in the State or Federal Courts to recover property; for in the event there subsequently be no adjudication, their right to sue in the ordinary tribunals would be undoubted; and they should not be prevented meanwhile from making use of the ordinary remedies for their protection, nor be deterred from doing so by any fear that subsequent adjudication of bankruptcy will not only rob them of all special advantage, but also throw the costs of suit upon them.⁷⁶

§ 1713. **Legal Proceedings Resulting in Recovery of Concealed Assets, etc., Creditor Entitled to Reimbursement.**—In the event the legal proceedings ultimately result in recovery of assets transferred or concealed by the bankrupt, the creditor will be entitled to reimbursement for his reasonable expenses in the suit.⁷⁷

This provision was added by the Amendment of 1903, yet, without it, it would doubtless have been true that such assets would have come into the bankruptcy court burdened with a lien in favor of the creditor through whose efforts and expense they were ultimately recovered. Such would be a logical deduction from the doctrine enunciated in *Randolph v. Scruggs*, 10 A. B. R. 1, 190 U. S. 533, where the Supreme Court held assets turned over by a state court assignee came into the bankruptcy court with such a lien upon them.

§ 1714. **Must Have Resulted to Benefit Estate, Else No Reimbursement.**—As was noted (ante, § 400), probably only those suits that were undertaken for the benefit of all creditors are strictly entitled to the benefits of § 64 (b) (2); yet the advantages of that section have been

⁷⁵. Bankr. Act, §§ 67 (f); 67 (b); 64 (b) (2). See "Creditors' Independent Plenary Suits Pending Adjudication," ante, § 399, et seq. See "Preservation of Liens for Benefit of Estate," § 1490.

Frost v. Latham & Co., 25 A. B. R. 313, 181 Fed. 866 (D. C. Ala.).

⁷⁶. But simple contract creditors

may not thus sue in the federal courts to set aside a fraudulent conveyance in aid of a pending bankruptcy petition even though diversity of citizenship exists. *Viquesnay v. Allen*, 12 A. B. R. 402, 131 Fed. 21 (C. C. A. W. Va.).

⁷⁷. Bankr. Act, § 64 (b) (2). See ante, § 399, post, § 2015.

extended to cases operating to the advantage of all creditors, although the cases were not so intended originally.⁷⁹ Thus, where an attachment lien, dissolved as to the attaching creditor by the debtor's bankruptcy, is preserved for the benefit of the estate under § 67 (f), the lien for the costs also is preserved.⁸⁰

§ 1715. Property Must Have Been "Transferred," or "Concealed" by "Bankrupt," Else No Reimbursement.—The wording of § 64 (b) (2) permitting reimbursement would seem to restrict the benefits of that section to cases of recovery of assets that had been transferred or concealed by the bankrupt, thus not covering cases of recovery of debts due the bankrupt or assets belonging to the estate not transferred or concealed by the bankrupt. Yet, it is considered that, under the doctrine of *Randolph v. Scruggs*, supra, and of the other cases cited supra, it is probable that, on showing made of benefit to the estate, reimbursement might be allowed in the latter cases as well.

§ 1716. Creditors May Not Bring Independent Plenary Actions in Bankruptcy Court.—But creditors, even though they may bring plenary actions, as above stated, nevertheless may not bring them in the federal courts of bankruptcy; for the jurisdiction conferred by the Amendment of 1903, upon the bankruptcy courts, to entertain plenary suits for the recovery of property, or its value fraudulently or preferentially transferred, authorizes only suits by trustees and not by creditors.⁸¹

§ 1717. Whether Receivers May Institute Plenary Suits for Property or Debts.—The receiver in bankruptcy has no title. He is simply custodian. And it has been held that he may not institute plenary suits for the recovery of property or debts.⁸²

Boonville Nat'l B'k v. Blakey, 6 A. B. R. 13, 107 Fed. 891 (C. C. A. Ind.): "The authority for the appointment of a receiver in bankruptcy proceedings comes from the act and is limited by the act. The order of the court appointing him cannot be broader than the statute. The receiver is a statutory receiver, and not a general receiver. The latter is appointed by a court of chancery by virtue of its inherent power, independent of any statute. His authority is derived from, and his duty prescribed by, the order of appointment, and he is called a common-law receiver. *Herring v. Railroad Co.*, 105 N. Y. 340, 12 N. E. 763. A statutory receiver is one appointed in pursuance of special

79. Compare, *In re Francis-Valentine Co.*, 2 A. B. R. 522, 94 Fed. 793 (C. C. A. Calif.).

80. *Receivers v. Staake*, 13 A. B. R. 281, 133 Fed. 717 (C. C. A. Va., affirmed sub nom. *First Nat. Bk. v. Staake*, 15 A. B. R. 639, 202 U. S. 141); *First Nat. Bk. v. Staake*, 15 A. B. R. 639, 202 U. S. 141.

81. Bankr. Act, § 23 (b) and § 70 (e). *Viquesnay v. Allen*, 12 A. B. R. 402, 131 Fed. 21 (C. C. A. W. Va.). Con-

tra, *Horner-Gaylord Co. v. Miller & Bennett*, 17 A. B. R. 257, 147 Fed. 295 (D. C. W. Va.). See ante, § 401. Also, compare, *In re Haupt Bros.*, 18 A. B. R. 585, 153 Fed. 239 (D. C. N. Y.).

82. *Beach v. Macon Grocery Co.*, 8 A. B. R. 751, 116 Fed. 143 (C. C. A. Ga.); *obiter*, *In re Kolin*, 13 A. B. R. 533, 134 Fed. 557 (C. C. A. Ills.); *Frost v. Latham & Co.*, 25 A. B. R. 313, 181 Fed. 866 (C. C. Ala.); also see ante, § 393.

statutory provisions. He derives his power from the statute, and to it must look for the duty imposed upon him. He possesses such power only as the statute confers, or such as may be fairly inferred from the general scope of the law of his appointment. We are therefore referred to the Bankrupt Act (30 Stat., ch. 541) to ascertain the powers of the bankruptcy court to appoint a receiver, and the extent of the power which the act confers upon him. * * * We can now discover, as we think, the general purpose of this law. It was that the property of the bankrupt should be vested in a trustee, to be selected by creditors; that such officer should have the general control and management of the estate, and the right to recover for the benefit of creditors all property transferred in fraud of the act. It contemplated that between the filing of the petition and the adjudication of bankruptcy an emergency might arise with respect to the care of the bankrupt's property; and in involuntary cases for the protection of the property in the interval between the filing of the petition and the adjudication, the bankruptcy court was authorized to direct the marshal to seize and hold the property pending adjudication. So, also, in voluntary or involuntary cases, when it was found absolutely necessary for the preservation of an estate, the court should appoint a receiver or the marshal to take charge of the property of the bankrupt until the petition is dismissed or the trustee is qualified. It plainly was not contemplated that the receiver or the marshal so designated should supersede the trustee or exercise the general powers conferred upon a trustee. There is no such power specifically conferred or any provision in the act from which such power can reasonably be implied. Such temporary receiver, whether he be the marshal or another, is not a trustee for the creditors, but is a caretaker and custodian of the visible property pending adjudication and until a selection of a trustee. If in any sense a trustee, he is trustee for the bankrupt, in whom is the title to the property until it passes by operation of law as of the date of adjudication to the trustee selected by the creditors. The duty required and the power conferred clearly are that the receiver or the marshal should take possession of the property that would otherwise go to waste, and hold it and preserve it, so that it might come to the trustee, when selected, without needless injury. There might also be an occasion when the business of the bankrupt ought not, in the interest of the creditors, to be temporarily suspended, as for example, in the case of a hotel or other business, where the value of the goods will require that it should be kept a going concern until the trustee should be appointed, and for a limited time after the trustee was appointed, that he might dispose of it profitably for the creditors."

In *re Schrom*, 3 A. B. R. 352, 97 Fed. 760 (D. C. Iowa): "Under these circumstances it is difficult to see how this court can exercise jurisdiction or control over the property in Illinois, or can confer any authority on the receiver to bring suit in Illinois against third parties to obtain possession of the property. The proper course to pursue is for the petitioning creditors to take proceedings in the proper court, State or Federal, in Illinois, in their own name, setting up the proceedings now pending in bankruptcy in this court as the basis of their action, and asking that court to protect the rights of the creditors in the property situated in Illinois, either by the appointment of a receiver, by injunction, or any other appropriate remedy. If the adjudication in bankruptcy is had, then the trustee who will be appointed can then appear in that case on behalf of the creditors, and take control of the proceedings."

Contra, obiter, In *re Fixen & Co.*, 2 A. B. R. 822, 96 Fed. 748 (D. C. Calif.): "The duty of a receiver is 'to take charge of the property of the bankrupts.' If an action at law or suit in equity is necessary to the accomplishment of that purpose, the receiver not only has the power, but it is his duty, to insti-

tute such action or suit. To say that he cannot resort to legal proceedings when necessary to take charge of the property of the bankrupt, while conceding that he may employ all other suitable agencies and instrumentalities for the purpose, is wholly illogical. Legal proceedings are sometimes the only means whereby the property of bankrupts can be preserved. Suppose that an estate consists of personal property, which has come into the hands of wrongdoers, who are about to secrete it or carry it beyond the jurisdiction of the court. Can it be seriously claimed in such a case that the receiver must sit quietly by and suffer the property to be irretrievably lost, on the ground that his functions are limited to the receipt of such property as may be voluntarily surrendered to him? The statement of the claim is its refutation. I hold that, it is clearly within the jurisdiction of the court appointing a receiver in bankruptcy to authorize him to institute necessary actions for the recovery of the bankrupt's property."

But where the receiver is duly authorized to maintain suits, his right to do so cannot be collaterally attacked even though the order were erroneous.⁸³

§ 1718. After Appointment of Trustee Suits Not to Be Instituted by Creditors.—After the appointment and qualification of the trustee suits may not be instituted by creditors to recover or protect assets for the estate, except in the trustee's name and when the court has authorized it upon the trustee failing to act. It is a general rule that after the appointment of the trustee all actions and proceedings for the recovery of property alleged to belong to the bankrupt estate must be brought by the trustee or in his name.⁸⁴

Compare, under law of 1867, *Glenny v. Langdon*, 98 U. S. 20: "1st. It is only through the instrumentality of his assignee that creditors can recover, and subject to the payment of their claims, the property which the bankrupt fraudulently transferred prior to the adjudication in bankruptcy, or which he concealed from and fails to surrender to his assignees."

Viquesnay v. Allen, 12 A. B. R. 402, 131 Fed. 21 (C. C. A. W. Va.): "Neither the original Bankruptcy Act nor the amendment seems to us to afford any ground for the contention of the appellee. The original act, § 23a, relates only to controversies between the trustee in bankruptcy and adverse claimants to property acquired or claimed by the trustee. So, also, 23b relates only to suits brought by trustees in bankruptcy. And the amendment, if applicable here, likewise only applies to suits by trustees in bankruptcy."

Smith v. Belden, 6 A. B. R. 423 (Supt. Ct. N. Y.): "His only interest is that of a general creditor in the successful prosecution of the action and in the dis-

⁸³ *Slaughter v. Louisville, etc., Co.*, 27 A. B. R. 570 (Sup. Ct. Tenn.).

⁸⁴ *Barnes Mfg. Co. v. Norden*, 7 A. B. R. 553 (Sup. Ct. N. J.); *In re Pearson*, 2 A. B. R. 821 (Ref. Pa.); *In re Carter*, 1 A. B. R. 160 (Ref. Ga.); *In re Rothschild*, 5 A. B. R. 587 (Ref. Ga.); *impliedly*, *In re Bailey*, 18 A. B. R. 226, 151 Fed. 953 (D. C. Penn.).

But compare instance where a judgment creditor was permitted to institute a suit after the debtor had been

adjudged bankrupt more than two months, to declare a fraudulent trust in property and to subject the same to the creditors' own judgment. *Evans v. Staalle*, 11 A. B. R. 182 (Supreme Court Minn.).

In re Meadows, Williams & Co., 25 A. B. R. 100, 181 Fed. 911 (D. C. N. Y.); and may sue surety on bond given for release of property. *Moore Bros. v. Cowan*, 26 A. B. R. 902 (Ala.).

position of its fruits. It is settled that on account of such interest he should not be made a party in the absence, as is the case upon this motion, of any allegations touching the good faith and diligence of the trustee for the creditors."

In *re Adams*, 1 A. B. R. 96 (Ref. N. Y.): "As has been seen, the Bankruptcy Act of 1898 not only vests in the trustee property fraudulently conveyed by a bankrupt, but, more than that, subrogates the trustee to all rights of creditors to recover such property. Under a provision of the former Bankruptcy Act (U. S., R. S., § 5046) vesting in the assignee under that act 'all property conveyed by the bankrupt in fraud of his creditors,' it was held, that the sole right to attack a fraudulent assignment, belonged to the assignee in bankruptcy; and it was repeatedly decided that it was only through the instrumentality of the assignee that a creditor could recover and subject to the payment of his debt property fraudulently transferred by a bankrupt prior to the adjudication of bankruptcy. *Olney v. Tanner*, 22 Blatchf. 540; *Glenny v. Langdon*, 98 U. S. 20; *Trimble v. Woodhead*, 102 U. S. 647; *Moyer v. Dewey*, 103 U. S. 301. In the case of *Olney v. Tanner*, it was further held, that all the creditor's right of action to reach such property passes to the assignee, now the trustee, as a statutory right, and he acquires not only all the rights of the creditor, but he is enabled to assail transfers which the creditor could not assail, unless he had acquired a right to or lien upon the specific property.

"If, by reason of their diligence in commencing their creditor's action before the filing of the petition in this case, and because the property fraudulently transferred was transferred before the passage of the act, the creditors opposing this motion have obtained equities superior to those of other creditors, undoubtedly they have no more to be lost under the provisions of the existing Bankruptcy Law than they were under the former law, under which it was held that the assignee took the estate in the plight in which he found it and subject to all vested liens and equities. *Yeatman v. Savings Institution*, 96 U. S. Rep. 764. Nor will those superior equities, if they exist, be lost when a trustee is appointed in this proceedings, because he will then be subrogated to the right of these creditors to prosecute their action."

§ 1719. Creditors Maintaining Suits in Trustee's Name.—Undoubtedly, creditors may maintain suits, using the trustee's name by leave of court, in cases where the trustee refuses or fails to act.⁸⁵

In *re Bailey*, 18 A. B. R. 226, 151 Fed. 953 (D. C. Penn.): "The order of the court is that upon the * * * filing of a bond in the court in the sum of five hundred dollars (\$500.00), conditioned for the payment of costs that may accrue in any litigation which the petitioner may require the trustee to institute for the recovery of property alleged to belong to the bankrupt's estate, that the trustee is hereby directed to institute such suits for the recovery of property as the petitioner and his counsel may direct, and any litigation so instituted to be directed and conducted for the trustee by petitioner's counsel; and it is so ordered."

And the court may require such creditors to indemnify the trustee against the costs and expenses of the litigation.⁸⁶

⁸⁵. See, on analogous subject of "Parties to Object to Claims," ante, §§ 824 and 826. Also, "Parties on Appeal," etc., post, § 2827, et seq.

⁸⁶. In *re Bailey*, 18 A. B. R. 226, 151 Fed. 953 (D. C. Penn.); In *re Meadows, Williams & Co.*, 25 A. B. R. 100, 181 Fed. 911 (D. C. N. Y.).

§ 1720. Trustee May Institute Suits for Recovery of Property.

—The trustee may himself, of course, commence and maintain suits for the recovery of property.

§ 1721. **May Sue in State Court.**—He may sue in the state court.⁸⁷ And in such case the local rules of pleading must be observed.⁸⁸

§ 1722. **May Sue without First Obtaining Leave.**—He may sue in the state court without first obtaining leave from the bankruptcy court.⁸⁹

Traders' Ins. Co. v. Mann, 11 A. B. R. 269, 118 Ga. 381: "There is a marked difference between the two (receiver and trustee). The powers of a receiver are not fixed by law but by the order of appointment. His duties vary in each case. In some instances they are active. He must operate a railroad, sell a stock of goods, manage a farm, or collect rents. He is often a mere stakeholder to preserve the property until final decree. He has no fixed duty or inherent power. Unless authorized so to do he has no right to bring suit. Civ. Code, 1895, §§ 4900, 4906. But the duties of a trustee in bankruptcy are fixed by statute. 'They shall collect and reduce to money the property of estates for which they are trustees'—words as fully warranting him to sue as an administrator, with the same power and duty. The fact that this is to be 'under the direction of the court' no more requires a preliminary order to sue than it would necessitate a special order to authorize him to go in person and present a note and demand payment. The money, when collected, after suit or without suit, and the use to be made thereof, was to be 'under the direction of the court.' But being bound to collect, he was not obliged

87. *Traders' Ins. Co. v. Mann*, 11 A. B. R. 269 (Sup. Ct. Ga.); *Chism v. Bank*, 5 A. B. R. 56 (Sup. Ct. Miss.); *In re Mersman*, 7 A. B. R. 46 (Ref. N. Y.); *Robinson v. White*, 3 A. B. R. 88 (D. C. Ind.); *Breckons v. Snyder*, 15 A. B. R. 112, 211 Penn. St. 176.

See for further instances the many cases cited under the subject of jurisdiction over adverse claimants: Subdivision "A," of this Division and Chapter, "Where Such Actions May Be Brought."

Instance, *Cohn, trustee, v. Small*, 18 A. B. R. 817, 120 App. Div. 211; instance, suing on bankrupt's contract for supplying money to manufacturing concern. *Monroe v. Bushnell*, 22 A. B. R. 587, 158 Mich. 115, 122 N. W. 508; *Drew v. Myers*, 22 A. B. R. 656, 81 Neb. 750, 116 N. W. 781, quoted at §§ 1687, 1692; *Hobbs v. Frazier*, 26 A. B. R. 887 (Sup. Ct. Fla.); instance, *Eichholz v. Polack*, 25 A. B. R. 243 (App. Div. N. Y.); instance, stockholder's liability for unpaid subscription, ante, § 976.

88. *Dreher Co. v. National Surety Co.* 27 A. B. R. 486 (Sup. Ct. Ala.).

89. *Callahan v. Israel*, 186 Mass. 383; *Chism v. Bank*, 5 A. B. R. 56 (Sup. Ct. Miss.), wherein the court held that it is incident to the trustee's right and

duty. Impliedly, obiter, *Hahlo v. Cohn*, 15 A. B. R. 592 (D. C. N. Y.).

But see contra, *In re Mersman*, 7 A. B. R. 46 (Ref. N. Y.): "Trustee should not begin suits to set aside alleged fraudulent or preferential transactions without applying for and obtaining the direction of the referee in charge. Such application should be made at some regular meeting of creditors."

But the trustee must get the approval of the bankruptcy court in advance where he seeks to be substituted for the bankrupt in a suit pending at the time of bankruptcy, see ante, § 899.

Objections of the secured creditor whose security is the object of attack are entitled to but little weight. *In re Mersman*, 7 A. B. R. 46 (Ref. N. Y.).

The trustee may be required to give security for costs in some States, when the cause of action arose before the bankruptcy, *Joseph v. Raff*, 9 A. B. R. 227 (Sup. Ct. N. Y. App. Div.); *Joseph v. Makley*, 8 A. B. R. 18 (Sup. Ct. N. Y. App. Div.); but compare, obiter, *In re Barrett*, 12 A. B. R. 626, 132 Fed. 362 (C. C. Tenn.).

Though, perhaps it is the better practice to obtain leave. *In re Meadows, Williams & Co.*, 25 A. B. R. 100, 181 Fed. 911 (D. C. N. Y.).

to secure a special order to bring suit necessary to collect. As to actions by or against the bankrupt pending at the time of the adjudication, the act requires him to obtain instructions from the court intervening. But the express requirement that he must obtain an order in such instances, while being silent as to the necessity therefore in cases like this, is conclusive that special permission was not necessary where he had to sue in order to collect a debt due the estate. The fact that the original Bankrupt Act (Act, March 2, 1867, ch. 176, 14 Stat. 517) required this action to be brought in a State court is here sufficient authority to begin this proceeding. Section 23b."

§ 1723. May Sue in Bankruptcy Court for Recovery of Property Transferred by Bankrupt.—He may also sue in the federal court, as we have seen ante, this Chapter, Division 2 (§§ 1684 et seq.), "In What Courts May Plenary Actions against Adverse Claimants Be Brought."⁹⁰

§ 1724. May Institute Suits against Debtors to Recover Money Judgments.—The trustee may institute suits to recover money judgments against debtors, and may maintain such suits already started by the bankrupt. He may sue in equity for an accounting.⁹¹

So, the trustee may proceed against a surety on a bond given for the release of property during the pendency of the bankruptcy proceedings.⁹²

§ 1724½. May Sue Creditors' Committee for Conversion of Assets.—It has been held that the trustee may sue a creditors' committee which has taken charge of the bankrupt's assets, sold them and attempted to administer the proceeds out of court, the bankrupt having absconded and of course not ratifying their agency.⁹³

DIVISION 4.

PLEADINGS AND PRACTICE IN PLENARY ACTIONS AGAINST ADVERSE CLAIMANTS TO RECOVER PROPERTY OR ITS VALUE.

SUBDIVISION "A."

NATURE OF SUCH ACTIONS.

§ 1725. Nature of Plenary Suits against "Adverse Claimants."
—Plenary suits against adverse claimants to recover property or its value transferred by the bankrupt, are generally in the nature of creditors' bills to set aside fraudulent or preferential transfers, and in general follow the

⁹⁰. And neither the trustee nor the receiver will be required to give security for costs nor to be personally liable therefor, unless acting in bad faith or unreasonably or oppressively; certainly not where there are assets in the bankrupt estate, nor where there are no assets, unless due in fairness to opposite parties to indemnify them against costs. In re Barrett, 12 A. B.

R. 626, 132 Fed. 362 (D. C. Tenn.). Also, see §§ 1684-1704, 1709.

⁹¹. Instance, *Monroe v. Bushnell*, 22 A. B. R. 587, 158 Mich. 115, 122 N. W. 508.

⁹². *Moore Bros. v. Cowan*, 26 A. B. R. 902 (Sup. Ct. Ala.).

⁹³. In re Thomas, 29 A. B. R. 945, 199 Fed. 214 (D. C. N. Y.).

rules of practice of such bills,⁹⁴ and the trustee is not confined to suits at law to recover the property or its value.

Pond v. N. Y. Exch. Bk., 10 A. B. R. 343, 124 Fed. 992 (D. C. N. Y.): "This suit is analogous to a judgment creditor's suit to set aside a fraudulent conveyance. The original payment when made was valid. It would not have been voidable by the bankrupt. It has only become voidable at the election of the trustee in bankruptcy, in the same manner as a fraudulent conveyance may be set aside by a judgment creditor. The jurisdiction in such cases has always been in equity. Many such suits in equity were brought by trustees in bankruptcy under the Act of 1867, for instance, *Grant v. National Bank*, 97 U. S. 80; *Rogers v. Palmer*, 102 U. S. 263; *Stucky v. Masonic Savings Bank*, 108 U. S. 74."

Lesser v. Realty Co., 17 A. B. R. 524, 116 App. Div. (N. Y.) 212: "The rule now seems to be well settled that whenever it is necessary, in an action of this character, to set aside a written instrument to enable the trustee to reclaim property unlawfully transferred, the action must be brought in equity and not at law."

Of course, the trustee may sue also on other causes of action than those for the recovery of property or its value; thus he may sue at law for a money judgment or in equity for an accounting, etc.⁹⁵

^{94.} *Parker v. Black*, 16 A. B. R. 203, 143 Fed. 560 (D. C. N. Y., affirmed in 18 A. B. R. 15, 151 Fed. 18).

Carter v. Hobbs, 1 A. B. R. 215, 92 Fed. 594 (D. C. Ind.): This case and the next, *Wall v. Cox*, are not, however, to be followed on the point that such suits could be brought in the bankruptcy court before the Amendment of 1903.

Wall v. Cox, 5 A. B. R. 727, 181 U. S. 244, reversing 4 A. B. R. 659, 101 Fed. 403; *Vollkommer v. Frank*, 14 A. B. R. 697, 107 App. Div. 594; *Bryan v. Madden*, 15 A. B. R. 388, 109 App. Div. 876; *Parker v. Black*, 18 A. B. R. 15, 151 Fed. 18 (C. C. A. N. Y., affirming 16 A. B. R. 202). *Obiter*, *Off v. Hakes*, 15 A. B. R. 700, 142 Fed. 364 (C. C. A. Ill.); *Andrews v. Mather*, 9 A. B. R. 301, 134 Ala. 358 (Sup. Ct. Ala.); *Beasley v. Coggins*, 12 A. B. R. 355, 48 Fla. 215 (Fla. Sup. Ct.); *Wall v. Cox*, 4 A. B. R. 659, 101 Fed. 403 (reversed, on other grounds, in 5 A. B. R. 527, 181 U. S. 244); impliedly, *Bardes v. Bank*, 4 A. B. R. 163, 178 U. S. 524; *Westall v. Avery*, 22 A. B. R. 673, 171 Fed. 626 (C. C. A. N. C.), quoted at § 1753.

Hobbs v. Frazier, 26 A. B. R. 887, — Fla. —. But the requirement that judgment must first be obtained, does not apply to a bill brought by the trustee to set aside a fraudulent conveyance.

Instance, *Allen v. Gray*, 24 A. B. R. 642, 139 App. Div. N. Y. 428. Apparent instance, *Gorham v. Buzzell*, 24 A. B. R. 440, 178 Fed. 596 (D. C. Me.).

Prior Agreement of Receiver to Sale by Adverse Claimant, Effect of.

Where the receiver in bankruptcy, not himself in possession, stipulates that the adverse claimant may himself sell the property involved, the trustee, subsequently instituting suit to set aside the original transfer to the adverse claimant, is, in general, bound by the price obtained. *Ommen, trustee, v. Talcott*, 23 A. B. R. 572, 175 Fed. 261 (D. C. N. Y.).

Bankruptcy Court Authorizing Receiver to Stipulate with Adverse Claimant for Sale of Property.

The bankruptcy court may authorize the receiver to make a stipulation for the sale by an adverse claimant of property in the possession of such adverse claimant. *Ommen, trustee, v. Talcott*, 23 A. B. R. 572, 175 Fed. 261 (D. C. N. Y.). And the trustee will be bound thereby, *ibid.*

Judicial Cognizance of State Exemption Laws.—The bankruptcy court will take judicial cognizance of state exemption laws. *In re Reed*, 26 A. B. R. 286, 191 Fed. 920 (D. C. Okla.).

^{95.} See ante, § 1724. *Gill Trustee v. Bell's Knitting Mills*, 24 A. B. R. 275 (N. Y. App. Div.), quoted at § 1728½.

§ 1726. Receivers May Be Appointed.—Receivers may be appointed therein.⁹⁶

Obiter, *Sheldon v. Parker*, 11 A. B. R. 170, 66 Neb. 630: "The trustee in a proper case may have a receiver pending the trial or pending an appeal, if the circumstances attending the case would entitle any other litigant to the same relief."

But a receiver will not be appointed to collect the rents and profits where the transferee is financially responsible.⁹⁷

§ 1727. Writs of Injunction and Sequestration Issuable.—Likewise, writs of sequestration or of injunction may be issued therein to take possession, or prevent the removal, of property.⁹⁸

§ 1728. Retransfer or Surrender of Choses in Action May Be Ordered.—Decrees for the re-transfer or surrender of choses in action may be made therein.⁹⁹

§ 1728½. May Sue in Equity for Accounting.—He may sue in equity for an accounting.¹

Gill, Tr., v. Bell's Knitting Mills, 24 A. B. R. 275, 137 N. Y. App. Div. 553: "If Henry H. Bell's Sons' Company had not gone into bankruptcy, clearly it could require an accounting by the defendant and payment by the latter of any surplus in its hands arising from the proceeds of the property transferred to it and the profits of the business conducted by it under the aforesaid agreements over and above what was necessary for the liquidation of the debts of Henry H. Bell's Sons' Company, except secured debts and debts in favor of A. E. Bell and W. M. Bell in accordance with the terms of the agreements. The plaintiff, having succeeded to the rights of the latter company under said agreements, is entitled to the same relief. It was held on the former appeal that the defendant must account. Even though there be no surplus in the hands of defendant after the complete execution of its trust, the plaintiff is nevertheless entitled to an accounting in order to have the defendant charged with the proper amount so as to minimize the claims it agreed to liquidate, which for

96. Compare, inferentially (where refused), *Rowland v. Auto. Car Co.*, 13 A. B. R. 799 (C. C. Pa.); *Cox v. Wall*, 3 A. B. R. 664, 99 Fed. 546 (D. C. N. Car., reversed, on other grounds, sub nom. *Wall v. Cox*, 5 A. B. R. 727, 181 U. S. 244, supra). Compare (where referee said to possess jurisdiction), *In re O'Brien*, 21 A. B. R. 11 (Ref. Mass.).

97. *Webb v. Manheim*, 16 A. B. R. 472, 109 App. Div. 63.

98. *Horskins v. Sanderson*, 13 A. B. R. 101, 132 Fed. 415 (D. C. Vt.); *Lawrence v. Lowrie*, 13 A. B. R. 297, 133 Fed. 995 (D. C. Mass.). Compare, *Rowland v. Auto. Car Co.*, 13 A. B. R. 799 (C. C. Penn.). Instance, *Blake v. Nesbet*, 16 A. B. R. 269, 144 Fed. 279 (D. C. Mo.).

As to whether injunction bond may

be dispensed with, see obiter, *In re Barrett*, 12 A. B. R. 627, 132 Fed. 362 (D. C. Tenn.).

Actual notice of granting of injunction sufficient to bind, *Blake v. Nesbet*, 16 A. B. R. 269, 144 Fed. 279 (D. C. Mo.). Analogously, *In re Krinsky Bros.*, 7 A. B. R. 535, 112 Fed. 972 (D. C. N. Y.).

99. *Bindseil v. Smith*, 5 A. B. R. 40 (N. J. Court App. & Err.). Impliedly, *Off v. Hakes*, 15 A. B. R. 700, 142 Fed. 364 (C. C. A. Ills.).

Ordering Preferred Creditor to Execute Re-Transfer of Real Estate.—Instance, *Lazarus v. Egan*, 30 A. B. R. 287, 206 Fed. 518 (D. C. Pa.).

1. Instance, *Monroe v. Bushnell*, 22 A. B. R. 587, 558 Mich. 115, 122 N. W. 508.

any unpaid balances will remain valid claims against the bankrupt estate in the hands of the plaintiff."

§ 1729. Trustee Not Confined to Suits in Equity, and in Proper Case May Sue at Law for Recovery of Property or Its Value.—The trustee is not confined to suits in equity; but in a proper case may sue at law for the recovery of the property or its value.²

Burns v. O'Gorman, 17 A. B. R. 815, 150 Fed. 226 (U. S. C. C. R. I.): "A trustee in bankruptcy may sue in trover for a conversion of goods occurring either after or before bankruptcy."

Obiter, Parker v. Black, 16 A. B. R. 204, 143 Fed. 560 (D. C. N. Y.): "It was not necessary for the trustee to invoke his equitable remedy: he was not exclusively confined to seek redress in a court of law. Either remedy apparently was open to the trustee in this case."

Thus, he may sue at law for the recovery of a preference.³

§ 1730. And Should Sue at Law unless Remedy Inadequate.—And the trustee should sue at law unless his remedy at law is inadequate.^{3a}

Warmcuth v. O'Daniel, 20 A. B. R. 101, 159 Fed. 87 (C. C. A. Tenn.): "The question on this appeal which arises on the first two of the assignments of error is whether the court below was right in overruling the appellant's contention on his demurrer that the suit was not properly brought in equity for the reason that there was a plain, adequate, and complete remedy by an action at law. The objection was taken at the threshold, and the question is not embarrassed by the laches of the defendant in raising it. We think the court should have sustained the demurrer. The judgment sought was for a definite sum of money, precisely that which the court by its decree awarded to the complainants. And the whole sum was recoverable, if any of it was; for the assets of the estate would not come near the amount of the debts. There was no contingency in the liability, or apportionment of the burden among several defendants to be made by the judgment. The response of the court to the demand of the complainants was simply an allowance or refusal of it. Nor was there any embarrassment in the procedure. The evidence produced would be, and was in this case, as completely available in an action at law as in a court of equity. No injunction was sought or required. The issue was one which a jury could readily understand and decide under proper instructions from the court in respect to the law. It

² *Wetstein v. Franciscus*, 13 A. B. R. 326, 133 Fed. 900 (C. C. A. N. Y.); instance, *Suffel v. McCartney Nat'l Bk.*, 16 A. B. R. 259, 106 N. W. (Wis.) 837; *Warmath v. O'Daniel*, 20 A. B. R. 101, 159 Fed. 87 (C. C. A. Tenn.), quoted at § 1730; *Cohn, trustee, v. Small*, 18 A. B. R. 817, 120 App. Div. N. Y. 211. Compare, *Johnson v. Hanley, Hoyer Co.*, 26 A. B. R. 748, 188 Fed. 752 (D. C. R. I.).

Jury trial to recover preference. *Newman v. Dry Goods Co.*, 31 A. B. R. 399 (Kansas City Court of Appeals).

Suing Debtors of Bankrupt after General Assignment Superseded by

Bankruptcy.—Practice: Demurrer to Petition: *Cohen v. Wagar*, 16 A. B. R. 381, 183 N. Y. 33.

Trustee Proper Plaintiff in Stockholder's Liability Suit, for Unpaid Stock Subscriptions.—*Thrall v. Union Mard Tobacco Co.*, 22 A. B. R. 287, 54 Ohio Law Bull. 732 (Ohio Com. Pleas.).

Lis Pendens of Trustee's Suit.—In re *Goldberg*, 22 A. B. R. 503 (N. Y. Sup. Ct.).

³ *Cohn, Trustee, v. Small*, 18 A. B. R. 817, 120 App. Div. N. Y. 211.

^{3a} *Johnson v. Hanley, Hoyer Co.*, 26 A. B. R. 748, 188 Fed. 752 (D. C. R. I.).

is suggested that the court must first set aside the transfer before it could proceed to judgment, and that it is the peculiar province of a court of equity to set aside unlawful transfers. This is an ingenious, but unsubstantial figment. No distinct or formal preliminary action was required or contemplated by the statute. If the defendant had obtained part of the estate which should have come to all the creditors, proof of that fact would entitle the trustees to recover it. Perhaps there may be cases where a declaration of the court may be necessary to completely fulfill all requirements, as where the transfer has been accomplished by a deed or other solemn instrument which may be made matter of record, or is a muniment of title the existence of which would indicate ownership and the right to sell and convey or mortgage, or do such other things with it as belong to ownership. But in the present case nothing is stated in the bill which makes such a proceeding necessary, nor indeed is anything more required than in any ordinary action at law where the plaintiff is always bound to establish the facts which create the liability, whereupon, and without more, the court gives judgment for the sum he is entitled to recover. And that was what occurred in the present instance. There was no preliminary declaration that this transfer be set aside. The suggestion made would be the adoption of a device for evading the statute forbidding a resort to a court of equity. The right of a defendant to have his liability determined in an action at law is a substantial one, the value of which is recognized and protected by the statute (§ 723, Rev. St.), which declares that 'suits in equity shall not be sustained in either of the courts of the United States in any case where a plain, adequate, and complete remedy may be had at law.' The defendant is thereby given an opportunity to have his controversy tried by a jury, a privilege of sufficient importance to be secured by the Constitution and guarded by this positive statute. * * * Even in cases of trust, when the conditions had been reduced to the simple fact that a certain sum of money was due from the trustee on account of his trust, a court of law was the proper forum, and a bill in equity would not lie."

But the defendant may waive the trial by jury;⁴ and the objection that the trustee does not sue at law comes too late when first made after submission of an adverse report of a special master.⁵

Objections to the charge to the jury can not be availed of unless exception was taken thereto.⁶

Sessler v. Nemcof, 25 A. B. R. 618, 183 Fed. 656 (D. C. Pa.): "If the trustee has an adequate remedy at law, a bill in equity cannot be maintained, in this or in any other court. Whatever equitable jurisdiction may have been conferred upon the District Court by the Bankruptcy Act and the amendments thereto, it is confined to controversies relating to a bankrupt estate. Within this limited area, whether or not a bill in equity may be maintained must be tested by the ordinary rules that govern bills before any other tribunal, and perhaps the most familiar test is to inquire whether the plaintiff has an adequate remedy at law."

§ 1730½. Facts Conferring Federal Jurisdiction to Be Pleaded and Proved.—Where the suit is brought in the United States District Court,

4. *Warmath v. O'Daniel*, 20 A. B. R. 101, 159 Fed. 871 (C. C. A. Tenn.).

5. *Mitchell v. Mitchell*, 17 A. B. R.

382 (D. C. N. Car., affirmed in 20 A. B. R. 924, 147 Fed. 280, C. C. A.).

6. *Gering v. Leyda*, 26 A. B. R. 137, 186 Fed. 110 (C. C. A. Neb.).

the facts conferring jurisdiction must be pleaded and proved;⁷ thus, either, that it is brought to recover property or the proceeds of property transferred by the bankrupt, fraudulently, preferentially or in such manner as that a creditor under state law might be entitled to recover the same;⁸ or that the property was in the custody of the bankruptcy court;⁹ or that the defendant is consenting to the jurisdiction;¹⁰ or that diversity of citizenship exists.

§ 1730³₄. **Special Masters.**—Where the suit is in equity, a special master may be appointed under the usual equity rules.¹¹

SUBDIVISION "B."

PLEADINGS AND PRACTICE IN ACTIONS BY TRUSTEES TO SET ASIDE FRAUDULENT TRANSFERS.

§ 1731. **Whether Petition to Show Inadequacy of Assets.**—It was formerly held that the petition must show that the trustee has not sufficient assets in his hands to satisfy creditors.¹²

Deland v. Miller, 11 A. B. R. 744, 119 Iowa 368: "Another aspect of the case is fatal to appellant's contention. He does not allege, nor did he offer to prove, that the assets in his hands were insufficient to satisfy the claims of all creditors. Under the Federal Bankrupt Act a trustee has power to avoid any transfer which any creditor might have avoided. A creditor could not have avoided this mortgage without showing some fraud as to him. The mortgage was good as between the parties, and, unless some one was harmed, it should be permitted to stand."

7. *Plaut, trustee, v. Gorham Mfg. Co.*, 23 A. B. R. 42, 174 Fed. 852 (D. C. N. Y.).

8. See ante, § 1692.

9. See ante, § 1692.

10. See ante, § 1692.

11. *Instance, Ommen, trustee, v. Talcott*, 23 A. B. R. 572, 175 Fed. 261 (D. C. N. Y.).

"Requests to Find Facts" Unknown in Federal Equity Practice.—*Ommen, trustee, v. Talcott*, 23 A. B. R. 572, 175 Fed. 261 (D. C. N. Y.): "'Requests to find facts' are, so far as I can find after considerable investigation, wholly unknown in equity practice in the Federal courts, and in this instance are undoubtedly borrowed from the practice of the New York Code, which was found once so intolerably burdensome as to be repealed, and which, having been now re-enacted, with the hope of giving a larger scope of review to the New York Court of Appeals, has again become a most vexatious annoyance to the judges. While, no doubt, only

those exceptions to the final report are good which were taken by objection to the draft report, the objections will themselves come up with the final report, and ordinarily will not be regarded at all, unless some point should be made as to the validity of the exceptions. It is, in my judgment, better that a report read as a narrative, and certainly it should not be cut up with statements as to what the master declined to find."

Proper Practice in Accounting before Special Master.—*Ommen, trustee, v. Talcott*, 23 A. B. R. 572, 175 Fed. 261 (D. C. N. Y.).

12. It has been held that where the schedules filed by the bankrupt declare that he has no assets, then such an allegation in the trustee's petition becomes unnecessary. In *re Schoenfield*, 27 A. B. R. 64, 190 Fed. 53 (D. C. W. Va.). But the obvious reply to such a holding is, that if it is necessary to allege and prove it, it ought to be alleged in the petition and be proved by competent evidence.

Mueller v. Bruss, 8 A. B. R. 442, 112 Wis. 407; "A third proposition is that the trustee cannot maintain this action unless it is shown by the complaint that he has not sufficient assets in his hands to satisfy the claims of the creditors of the debtor. No such showing is made in the complaint. For all that appears therein, there may be money and property enough in his hands to pay every claim against the debtor. The conveyances attacked were good between the parties thereto. *Ellis v. Land Co.*, 108 Wis. 313, 84 N. W. 417. Third parties are not allowed to impeach them unless it is necessary to do so in order that justice may be done. The trustee has no right superior to that of the creditors he represents. If we admit that the facts stated show such transfers to have been fraudulent, still no right to avoid them exists unless it appears that some one was harmed. It seems quite evident, without argument, that unless it is made to appear that the property so conveyed is needed to pay the claims filed against the debtor, the trustee has no right to set such conveyances aside. The complaint is insufficient in this respect. It ought to show the amount of claims filed, and the value of the assets in his hands, so that the court may determine the necessity of resorting to this proceeding. Its infirmity in this respect renders it susceptible to the demurrer."

Prescott v. Galluccio, 21 A. B. R. 229, 164 Fed. 618 (D. C. N. Y.): "It must appear that the property of the bankrupt is not sufficient to pay his creditors in full. This should be alleged and there will be an amendment accordingly."

Although compare, apparently but not really contra, *Breckons v. Synder*, 15 A. B. R. 112, 211 Pa. St. 176: "The adjudication was evidence of the bankrupt's insolvency at its date, and it was not necessary to prove insolvency at the trial."

However, since the Amendment of 1910 to § 47a (2) endowing the trustee with the rights and remedies of a creditor "armed with process," such averment and proof may not be necessary.

Kraver v. Abrahams, 29 A. B. R. 365, 203 Fed. 782 (D. C. Pa.): "The defendant demurs upon the ground that the statement contains no averment that the trustee, the plaintiff, has not sufficient assets on hand to pay all of the bankrupt's creditors in full, relying upon the cases of *Mueller v. Bruss*, 9 A. B. R. 442, 112 Wis. 406, 88 N. W. 229, and *Prescott v. Galluccio* (D. C. N. Y.), 21 A. B. R. 229, 164 Fed. 618, in which it was held that in a suit to set aside a transfer of property by the bankrupt upon the ground that it was fraudulent as to creditors, the trustee must aver and prove that the property of the bankrupt is not sufficient to pay his creditors in full. The rule laid down in the cases cited was based upon the ground that the trustee has no rights superior to the creditors whom he represents and that even if the transfer is fraudulent there is no right to avoid it unless it appears that the assets of the bankrupt estate are insufficient to pay the creditors in full. The necessity, if it existed, to aver and prove a deficiency of assets appears, however, to have been removed by the amendment of 1910 to § 47a (2) of the Bankruptcy Act by which it is provided that as to all property not in the custody of the bankruptcy court the trustee shall be deemed vested with all the rights, remedies and powers of a judgment creditor holding an execution returned unsatisfied. In other words, under the amendment where a transfer is alleged to have been fraudulent as to creditors and insolvency is alleged to have existed at the time, the trustee is in the position of a creditor who has proved by an execution returned unsatisfied that a deficiency of assets exists. There is, therefore, no necessity for its averment in the statement of claim."

And, of course, inadequacy of assets need not be alleged where the action is one which the bankrupt himself might have maintained.

Drew v. Myers, 22 A. B. R. 656, 81 Neb. 750, 116 N. W. 781: "Where a trustee in bankruptcy seeks to recover the property of the bankrupt in an action which the bankrupt might have prosecuted but for the intervention of the bankruptcy, he is not required to allege that he has not sufficient assets of the estate in his hands to pay the liabilities thereof. Such allegation is only necessary when the action is brought to avoid a preference or fraudulent conveyance made by the bankrupt. The rule enunciated in *Flint v. Chaloupka* and the cases cited to support the same is restricted to cases brought by the trustee to avoid preferences or to recover property converted by the bankrupt in fraud of the creditors. The reason for the rule is that such actions are essentially in the nature of creditors' bills, and the insufficiency of the property left in the debtor's hands after making fraudulent conveyances is an essential element of the right of the creditor to question such conveyances. Here the plaintiff claims that defendant's father, who was an officer of the bankrupt corporation, taking advantage of this position, withdrew or possibly embezzled some \$500 of its funds, which he turned over to the defendant, his son, and which was by him deposited in the defendant bank. In such a case the bankrupt, but for the appointment of the trustee could have maintained this action to recover such money. We think it safe to say that the trustee of a bankrupt may maintain any action which the bankrupt might have maintained but for the intervention of the bankruptcy, and that it is not necessary in such a case for him to state that the property already in his hands is insufficient to pay the debts of the bankrupt. It is only when he brings an action which is in the nature of a creditor's bill that he is required to make such allegation."

But at any rate it is no defense to an action by a trustee that the trustee might recover against officers and directors for dereliction of duty and against stockholders for unpaid subscriptions.

In *re Standard Tel. & Elec. Co.* (*Knapp v. Milw. Tr. Co.*), 216 U. S. 545, 24 A. B. R. 761, quoted further at § 1207¼ and § 1258: "In *Mueller v. Bruss*, 8 Am. B. R. 442, 112 Wis. 406, it was held that a trustee in bankruptcy could maintain an action to set aside a fraudulent conveyance, but that the complaint must aver and the trustee must show that the estate had not sufficient assets in the trustee's hands to satisfy the claims filed against the debtor. And, it is insisted, that a showing of this character is lacking in the present case. Without deciding that under the Bankruptcy Act the answer of the trustee in bankruptcy was required to make this averment, accompanied by proof, if necessary, it is sufficient upon this point to say that the intervening petition of the trustee of the mortgage sought to assert a lien upon all the property of the bankrupt in the trustee's hands. The suggestion in appellant's brief, that the trustee in bankruptcy may possibly recover against directors and officers of the corporation for dereliction of duty, and against stockholders for unpaid subscriptions and additional liability on their part, presents no reason why he may not resist an attempt to take all the available property in his hands to apply on a mortgage void as to creditors at the time of the adjudication."

§ 1732. Return of Execution Unsatisfied, Not Always Prerequisite.—It was held in some cases, even before the Amendment of 1910 to Bankr. Act, § 47 (a) (2), that the obtaining of judgment and issuance and

return of execution unsatisfied as evidence of exhaustion of legal remedies might be excused.¹³

Mueller v. Bruss, 8 A. B. R. 442, 112 Wis. 406: "Obtaining judgment on the claim with a return of an execution unsatisfied, is prima facie evidence of the exhaustion of all legal remedies against the debtor. The rule stated, however, is not inexorable and without exceptions. If it appears that for any reason a judgment against a debtor cannot be obtained, it will be excused as a preliminary to a creditors' suit. *Smith Eq. Rem. of Cred.*, § 167. The exceptions noted and discussed in the book last referred to, fairly illustrate the law on that subject. The principle involved in the exceptions to the rule is that when a party has done all that is possible for him to do to prepare his case for equitable cognizance, he is not to be denied access to the only tribunal capable of granting relief. This leads us to the consideration of the situation presented by the allegations of the complaint. It is not alleged that any of the creditors have ever obtained judgment on their claims. The trustee has not secured a judgment, and it is not perceived how either he or the creditors could do so, under the provisions of the Bankrupt Act. By section 11 all suits founded on a claim from which a discharge would be a release, pending at the time of the petition, are to be stayed until after an adjudication or the dismissal of the petition, and, if such person be adjudged a bankrupt, such suits are to be stayed until 12 months after the date of such adjudication, or, if within that time such person applies for a discharge, then until the question of such discharge is determined, so that, unless the creditor had obtained a judgment before petition filed, he could not do so until after a discharge. Such discharge releases the bankrupt from all provable debts except such as are mentioned in § 17. In the meantime the trustee is vested with all the rights the creditors had to avoid transfers made by the debtor. The creditors could not sue and obtain judgment pending the bankruptcy proceedings. The trustee had no greater right. Hence, by the operation of a paramount law of the United States, the creditors were prevented from obtaining a judgment upon which to base the right to attack the conveyance of their debtor, alleged to have been fraudulently made. This brings the case within the exception before mentioned, and excuses the trustee from obtaining a judgment and issuing execution as a preliminary to the suit."

Compare, *Brown v. Barker*, 8 A. B. R. 450, 458, 68 App. Div. 594, 74 N. Y. Supp. 43: "The courts are not inclined to extend the cases in which a plaintiff will be excused from pursuing the ordinary course of obtaining a judgment upon his indebtedness, and we think that it will not be going too far to hold that a plaintiff seeking to make such an excuse as is urged in this case shall clearly allege and show that the restraining order has been made against his opposition and without his procurement or consent."

In *re Martin*, 5 A. B. R. 424, 105 Fed. 723 (D. C. N. Y.): "Is it essential that the plaintiff proceed to judgment, and exhaust his remedy in the manner specially pointed out by the undertaking? I am clearly of the opinion that it is not necessary. The plaintiff, by the restraining order of the bankruptcy

13. *Platt, Assignee, v. Matthews*, 10 Fed. 280 (D. C. N. Y.); *Thomas v. Roddy*, 19 A. B. R. 873, 122 N. Y. App. Div. 851; obiter, *Ryker v. Gwynne*, 21 A. B. R. 95 (N. Y. Sup. Ct. Special Term).

But compare, *Viquesney v. Allen*, 12 A. B. R. 402, 131 Fed. 21 (C. C. A. W. Va.): This was a peculiar case. A simple contract creditor undertook

after the involuntary proceedings had begun although before adjudication, to institute an independent suit in aid of the bankruptcy proceedings, as ancillary thereto, to set aside an alleged fraudulent conveyance. The court held two points: a simple contract creditor could not maintain the action, and that a creditor was not the proper party, in any event.

court, is prevented from proceeding to judgment and execution in the pending suit before the justice of the peace by the paramount authority of the bankruptcy court. This court has power to stay pending suits founded upon a claim for which a discharge would be a release. The performance of the conditions imposed on the plaintiff in the suit by virtue of the stay becomes impossible, and the discharge of the bankrupt from his debts has the same effect as the return of an execution wholly or partly unsatisfied."

Beasley v. Coggins, 12 A. B. R. 355, 57 So. Rep. 213 (Sup. Ct. Fla.): "The general rule is that, before a creditor can maintain a bill in equity to set aside a conveyance by his debtor of his real estate on the ground of fraud, the creditor must reduce his claim to judgment, or its equivalent, a decree for a balance remaining after a foreclosure sale of mortgaged property, creating a lien on such real estate; and, when personal property or equitable assets are pursued, he must have an execution issued and returned *nulla bona*. *Robinson v. Springfield Company*, 21 Fla. 203. But does this rule apply to such a suit by a trustee in bankruptcy? * * * Section 70e * * * was intended to provide simply that the trustee in bankruptcy should have the same right to avoid conveyances as was possessed by creditors, or any of them, and this with especial reference to the statute of 13 Elizabeth. Under the Bankruptcy Act, when one is thereunder adjudged a bankrupt creditors are not permitted to attack fraudulent conveyances of their debtor, made more than four months of the adjudication of bankruptcy; and, if the trustee could not do so, then the act would constitute 'a device to permit fraudulent conveyances to take effect with impunity in case they are successfully concealed for the specified four months.' * * * The case of *Platt, Assignee v. Matthews* (D. C. N. Y.) 10 Fed. 280, arose under the bankrupt law previous to that of 1898. A bill was filed by the assignee to reach property alleged to have been fraudulently transferred by the bankrupt. It was contended on demurrer that, as no creditor had a judgment and execution against the bankrupt, such a bill would not lie. The court held that, inasmuch as the Bankruptcy Act vested the assignee with the title of all property conveyed by the bankrupt in fraud of creditors, the assignee acquired his rights through the act, and not through what had been done by the creditors. The court overruled the demurrer.

"In *Bump on Fraudulent Conveyances*, § 553, it is stated that, in order for an assignee in bankruptcy to maintain a bill to set aside a fraudulent conveyance, it is not necessary that he shall have a lien on the property, and obtain a return of *nulla bona*. In *Cady v. Whaling*, 7 Biss. 430, Fed. Cas., No. 2,285, an assignee in bankruptcy filed a bill to set aside a fraudulent conveyance made before the Bankrupt Act was passed. It was contended that such a bill could not be maintained on behalf of general creditors who had no specific lien. The contention was overruled."

The Amendment of 1910 to the Bankruptcy Act, § 47a (2), endowing the trustee with the attributes of a "creditor armed with process" is conclusive on the right of the trustee to maintain such actions as would have required the obtaining of a judgment and the return of an execution unsatisfied. Thus, in jurisdictions where such return of execution is essential in order to pursue conspirators collusively transferring and concealing assets.

Sattler v. Slonimsky, 28 A. B. R. 729, 199 Fed. 592 (D. C. Pa.): "This action in trespass is brought to recover damages arising from an alleged unlawful

conspiracy entered into by the defendants prior to the adjudication in bankruptcy to fraudulently and collusively transfer and conceal moneys of Harry Ruderman and Jacob Ruderman, the bankrupts for the purpose of hindering and delaying their creditors.

"Prior to the amendment of June 25, 1910 to § 47a of the Bankruptcy Act, such a suit could not have been maintained upon a cause of action arising prior to the adjudication in bankruptcy because the rights of action which vested in the trustee upon his appointment were only such as were vested in the bankrupts prior to the adjudication. The amendment to § 47a provides, however, that the trustee 'as to all property not in the custody of the bankruptcy court shall be deemed vested with all the rights, remedies, and powers of a judgment creditor holding an execution duly returned unsatisfied.'

"That a creditor may bring an action of trespass on the case upon a conspiracy to fraudulently secrete and transfer the property of a defendant in an execution from the reach of the plaintiff is well settled."

Thus, also, to recover fraudulent transfers.¹⁴

§ 1733. Insolvency Not Necessary Where Actual Intent to Defraud Proved.—It is not necessary to show insolvency if an actual intent to hinder, delay and defraud is proved without showing insolvency, unless the action be brought under a statutory provision requiring such showing.¹⁵

§ 1734. "Insolvency," Here Means Inadequacy of Assets, Not Mere Inability to Pay "In Due Course."—"Insolvency," as understood in dealing with contracts or conveyances challenged on the ground of fraud, actual or constructive, has reference to insufficiency of assets to cover liabilities, even in jurisdictions where the term "insolvency," as understood in the administration of insolvency laws, is the inability of the debtor to pay his debts as they mature in the regular course of business.¹⁶

§ 1734¼. Whether Exempt Property Included Determined by State Law.—Whether exempt property is to be included or excluded in the estimate of the assets in such suits is to be determined by state law.^{16a}

§ 1734½. Allowance of Claim, Subrogation and Reimbursement of Transferee on Setting Aside Constructively Fraudulent Transfer.—On the setting aside of a transfer which is not actually fraudulent, but

14. *Kraver v. Abrahams*, 29 A. B. R. 365, 203 Fed. 782 (D. C. Pa.), quoted ante, § 1731.

15. Inferentially, *Lansing Boiler Wks. v. Ryerson & Son*, 11 A. B. R. 560, 128 Fed. 701 (C. C. A. Mich.). Inferentially (this being a case where the fraud was urged as an act of bankruptcy), *In re Pease*, 12 A. B. R. 66, 129 Fed. 446 (D. C. Mich.). Inferentially, *In re Steininger Mercantile Co.*, 6 A. B. R. 68, 107 Fed. 669 (C. C. A. Ga.).

16. *Marvin v. Anderson*, 6 A. B. R. 520, — Wis. —, 87 N. W. 226.

Sales by Insolvent Corporations.—"Trust fund" doctrine, so-called, has no application to a going corporation.

Its creditors have no equitable lien upon its assets. Such lien does not attach till the corporation is insolvent and has either suspended business or is on the verge of collapse, so that it may reasonably be said to be civilly dead as regards the purposes for which it was organized. *Marvin v. Anderson*, 6 A. B. R. 520, 87 N. W. 226, — Wis. —.

Presumption of Authority of Officers of Corporation.—The presumption is that the officers were authorized to execute the transfer. *Marvin v. Anderson*, 6 A. B. R. 520, 87 N. W. 226, — Wis. —.

16a. *Underleak v. Scott*, 23 A. B. R. 926, 136 Minn. 117.

merely constructively so, the claim of the transferee has been allowed; and he has been subrogated to the rights of those who had received the consideration paid by him, less deduction of the expense of setting aside the transfer.¹⁷

Barber v. Coit, 16 A. B. R. 419, 144 Fed. 381 (C. C. A. Ohio): "In order to set aside a transfer under this section (§ 6343, Rev. Stats. Ohio) it is not necessary that actual fraud or intent to defraud be shown. The intent to prefer is made constructively fraudulent and renders the transfer voidable. * * * This is a finding that the sale was made to prefer certain creditors and therefore was constructively fraudulent. It goes no further. * * * Under these circumstances, since the creditors have received the full benefit of the money which Coit paid to Payne, and since Coit has nothing to show for this money, the property which he received in exchange having been taken away from him and handed over to the trustee for the benefit of the creditors, it seems to us that Coit has a valid claim against the trustee for the full amount of the money he paid, less the expenses of setting aside the sale. The creditors lose nothing they are justly entitled to by giving up the money, for they have the property, and it would be manifestly inequitable for them to hold both property and money."

And such fraudulent transferee has been allowed reimbursement or offset for taxes, repairs and interest actually paid by him.¹⁸

§ 1735. Pleadings to Show Trustee's Representative Capacity.—The pleadings of course must show that the trustee sues in his representative capacity. But the title and pleadings may be considered together to determine the capacity. Thus, where the title simply shows "trustee" but the petition clearly shows he sues in his representative capacity "as trustee," it will not be construed as *descriptio personæ* merely.¹⁹

§ 1736. Trustee Presumed to Represent Creditors and to Be Authorized to Act; Though No Claims Proved.—The trustee may sue although no claims are proved by creditors in the bankruptcy proceedings. The trustee is entitled to institute and maintain a suit to set aside an alleged fraudulent conveyance even though no creditor has proved his claim in the bankruptcy proceedings. He is presumed to represent creditors, and the burden of proof of rebuttal is upon those who deny his authority.

Oliver v. Hilgers, 11 A. B. R. 178, 92 N. W. 911 (Minn.): "We think it is necessarily implied from the language and spirit of that act that the trustee is empowered to proceed to protect the rights of creditors, and to take possession of all property of the bankrupt, without waiting for any proof to be filed by any particular creditors, and that, when it appears that such trustee has been appointed in voluntary bankrupt proceedings, it will be presumed that he represents creditors; and will also be presumed that the creditors in existence at the time of filing the petition were not paid subsequently, and the burden was upon appellants to show the contrary."

17. See ante, § 775. See also, §§ 767¾, 1227½; In re Clark, 24 A. B. R. 388, 176 Fed. 955 (D. C. N. Y.), quoted at §§ 727½, 1227½.

18. In re Chase, 13 A. B. R. 294, 133 Fed. 79 (D. C. Mass.).

19. *Newland v. Zodikow*, 11 A. B. R. 770, 39 Misc. 541, 80 N. Y. Supp. 375.

But compare, inferentially, contra, but obiter, *Breckons v. Snyder*, 15 A. B. R. 115, 211 Pa. St. 176: “* * * It is argued that it was incumbent on the plaintiff to show that there were unsatisfied creditors at the time of the transfer, at the time the suit was brought, and at the time of the trial, for the reason that, if there were no creditors when the transfer was made, there was no one to be defrauded by it, and if there were none afterwards there was no one in whose interest the trustee could maintain the action. The first ground of objection would not be without merit if a recovery had been sought because of a preferential transfer within the time prohibited by law. But the second count was withdrawn, and the only issue at the trial was whether a debt had existed and had been paid. No other right to retain the money was set up. If it had not been given to the defendant in discharge of a debt, it was the bankrupt’s money in the defendant’s hands, which the trustee could recover for creditors.”

The presumption is that the trustee has complied with all the requirements of the Bankrupt Act and is qualified to act, although the record does not show he has obtained an extension of time for filing his bond after the expiration of the time provided by the Bankrupt Act.²⁰

The defendant may set up, however, that certain alleged creditors failed to file their claims in the bankruptcy proceedings in the time allowed therefor, and were therefore barred from participation in the distribution of the bankrupt’s estate, and that there can be no recovery by the trustee for the benefit of such creditors.²¹

§ 1737. Tender of Actual Consideration Paid, Not Necessary.—The tender of the actual consideration paid which is necessary in a suit to rescind a sale between the vendor and vendee, need not be alleged where the bill sufficiently alleges a sale for an inadequate consideration with intent to hinder, delay or defraud creditors, participated in by the purchaser. Whether refund of any part will finally be decreed is to be determined later.²²

§ 1738. Whether Transfer Voidable Only as to Some Creditors, Nevertheless, Avoided as to All.—Where a transfer which is not void as to all creditors but only as to a part of the creditors, is set aside and thereby property recovered, it is probable that, in the absence of local law to the contrary, the transfer being set aside, it is set aside for all purposes and all creditors are entitled to share therein, although as to some so sharing the transfer would not have been void.²³ The bankrupt law entitles the trustee to avoid for the benefit of all creditors any transfer which any creditor might have avoided.²⁴ The estoppel of some creditors

20. *Breckons v. Snyder*, 15 A. B. R. 115, 211 Pa. St. 176.

21. *Cartwright v. West*, 26 A. B. R. 831, 173 Ala. 198.

22. *Johnson v. Forsythe Mercantile Co.*, 11 A. B. R. 673, 127 Fed. 845.

23. See ante, §§ 1140, 1225½, 1265. Also, *In re Gray*, 3 A. B. R. 647, 62 N.

Y. Supp. 618; (1867) *Smith v. Kehr*, 7 Nat. Bank Reg. 97; *In re Duggan*, 25 A. B. R. 479, 183 Fed. 405 (C. C. A. Ga., affirming 25 A. B. R. 105).

24. Bankr. Act, § 70 b. *In re Hurst*, 26 A. B. R. 781, 188 Fed. 707 (D. C. W. Va.); *Washington v. Tearney*, 27 A. B. R. 651, 194 Fed. 830 (C. C. A. W.

does not necessarily work an estoppel of the trustee.²⁵

However, this is largely a matter of state law.²⁶ In states where the law makes such a distinction, it has been held that the petition or bill is demurrable unless it sets forth the debts and the dates of their creation.²⁷

§ 1739. Charging Same Transaction in Alternative, Fraudulent or Preferential, Not Inconsistent.—The joinder of a fraudulent conveyance and a voidable preference, alleged as to the same facts, is not a joinder of inconsistent causes of action.²⁸

But of course it would be different if the fraudulent conveyance were alleged to be wholly without consideration. Such a conveyance would be inconsistent with a preference, for a preference can only be made to a creditor.

§ 1740. All Matters Proper in Creditor's Bill, Proper Here.—All matters and causes of action proper in a creditor's bill are proper in an action brought by the trustee in the bankruptcy court to set aside a fraudulent transfer.²⁹

§ 1741. Both Bankrupt and Transferee in Fraudulent Transfer Proper Parties, Though Bankrupt and Intermediate Transferee Not Necessary.—Both the transferor and the transferee in an alleged fraudulent transfer are proper parties, though charged with different acts of fraud affecting different parts of the estate, their acts having been done with a common fraudulent purpose;³⁰ but the bankrupt is not a necessary party;³¹ nor is a fraudulent transferee who has transferred to another fraudulent transferee all the property rights received under the transfer a necessary party.³²

§ 1742. Several Acts Committed with Common Design, Joinable.—A bill is not multifarious if it join different defendants charged with different acts of fraud affecting different portions of the estate, provided it shows that they were committed with a common fraudulent purpose and

Va.). But compare, *contra*, *In re Cannon*, 10 A. B. R. 64, 121 Fed. 582 (D. C. S. C.).

25. Compare, inferentially, but not directly in point, *Frank v. Musliner*, 9 A. B. R. 230 (N. Y. Sup. Ct. N. Y., 76 N. Y. App. Div. 617).

26. Impliedly, *In re Kohler*, 20 A. B. R. 89, 159 Fed. 871 (C. C. A. Ohio), quoted at § 1225½. But compare, *Moore v. Green*, 16 A. B. R. 48, 145 Fed. 480 (C. C. A. W. Va.).

27. *Teague v. Anderson Hdw. Co.*, 20 A. B. R. 424, 161 Fed. 165 (D. C. Ga.).

28. *Kraver v. Abrahams*, 29 A. B. R. 365, 203 Fed. 782 (D. C. Pa.); *Grant v.*

Nat. Bank, 28 A. B. R. 712, 197 Fed. 581 (D. C. N. Y.); *Bryan v. Madden*, 11 A. B. R. 763, 78 N. Y. Supp. 220; *Wright v. Skinner*, 14 A. B. R. 500, 136 Fed. 694 (D. C. N. Y.); *Pratt v. Christie*, 12 A. B. R. 1 (N. Y. Sup. Ct., 95 App. Div. 282). Compare instance, but no ruling made, *Laundy v. Nat'l Bk.*, 11 A. B. R. 223, 66 Kan. 759.

29. *Carter v. Hobbs*, 1 A. B. R. 215, 92 Fed. 594 (D. C. Ind.).

30. *Carter v. Hobbs*, 1 A. B. R. 215, 92 Fed. 594 (D. C. Ind.).

31. *Cox v. Wall*, 3 A. B. R. 664, 99 Fed. 546 (D. C. N. Car.); *French v. Smith*, 4 A. B. R. 785 (Sup. Ct. Minn.).

32. *Skillen v. Endelman*, 11 A. B. R. 766, 79 N. Y. Supp. 413.

that the object of the suit is simply to wipe out the fraud, clear the title and recover the value of the property for the creditors, the fraud, as alleged, relating to the same general subject in which each defendant has a common interest, centering in the real point in issue.³³

§ 1742½. **Conspiracy to Defraud.**—Action may be brought against several for conspiracy to defraud creditors;³⁴ and the petition will not be demurrable for failure to specify which one of them actually received the property.³⁵

But if such action be one merely to recover general damages for the conspiracy rather than for the recovery of property or the proceeds of property wrongfully transferred by the bankrupt, it may not be brought in the District Court.³⁶

§ 1743. **Property to Be Shown to Belong to Estate.**—The property involved must be shown to be of a kind that would pass to the trustee;³⁷ that is to say, to be such as, but for the transfer complained of, could have been transferred or seized by legal process at the time of the filing of the bankruptcy petition. Thus, in the case of the fraudulent transfer by a bankrupt beneficiary of an insurance policy on the life of another, the petition must show that such beneficiary's interest was of a kind that made it transferable by some means or leviable upon at the time of the bankruptcy.³⁸

§ 1744. **Fraudulent Intent to Be Alleged and Proved.**—Fraudulent intent must be alleged and proved.³⁹

§ 1745. **Fraud, a Question of Fact.**—"Fraud" is a question of fact⁴⁰ to be deduced from the surrounding circumstances.⁴¹

§ 1746. **Burden of Proof.**—The burden of proof is, of course, on the

33. *Carter v. Hobbs*, 1 A. B. R. 215, 92 Fed. 594 (D. C. Ind.).

34. See post, § 2328½.

35. *Strasburger v. Bach*, 19 A. B. R. 732, 157 Fed. 918 (D. C. Ills.).

36. Compare, ante, §§ 1213¾, 1692, 1694. Also see *Lynch v. Bronson*, 24 A. B. R. 513, 177 Fed. 605 (D. C. Conn.), quoted at § 1694.

37. *In re Leech*, 22 A. B. R. 599, 171 Fed. 622 (C. C. A. Ky.).

38. *Carr v. Myers*, 15 A. B. R. 116, 211 Penn. St. 349.

39. *Halbert v. Pranke*, 11 A. B. R. 620 (Sup. Ct. Minn.); impliedly, *Hazard v. Wight*, 25 A. B. R. 883 (App. Div. N. Y.); *Grinstead v. Union, etc., Co.*, 27 A. B. R. 123, 190 Fed. 546 (C. C. A. Wash.); *Silling v. Todd*, 27 A. B. R. 127 (Sup. Ct. Va.); *Underleak v. Scott*, 28 A. B. R. 926 (Sup. Ct. Minn.);

Van Iderstine v. Nat. Discount Co., 29 A. B. R. 478, 227 U. S. 575, quoted at § 1221.

40. *Sherman v. Luckhardt*, 9 A. B. R. 307, 65 Kans. 610 (overruled, on other grounds, by same court, in 11 A. B. R. 26); *Peterson v. Mettler*, 29 A. B. R. 158, 198 Fed. 938 (D. C. Wash.).

Provinces of Court and Jury.—Where the principal witness for the plaintiff has given substantial testimony upon the issue to which the jury might in the proper exercise of its function give credit, it is error to direct a verdict for defendant upon the ground that the witness, in the opinion of the trial judge, was not worthy of belief. *Waters v. Davis*, 16 A. B. R. 667 (C. C. A. Tenn.).

41. *In re Elletson Co.*, 23 A. B. R. 530, 174 Fed. 859 (D. C. W. Va.).

trustee;⁴² except that when brought under § 67 (e), the burden of proving the good faith of the transferee is on the transferee.⁴³

§ 1747. Schedules and General Examination of Bankrupt Inadmissible against Transferee.—The schedules of the bankrupt are inadmissible against the transferee: they are not his admissions.⁴⁴ Likewise, the general examination of the bankrupt is inadmissible.⁴⁵

Taylor v. Nichols, 23 A. B. R. 310, 134 App. Div. (N. Y.) 787: "These schedules and part of the evidence so given by him in the bankruptcy proceeding were offered in evidence by the plaintiff upon the trial for the purpose of establishing the insolvency of the said Nichols at that time. To this offer the defendant objected, that as to him they were hearsay and that he was not bound by these declarations. The objections were overruled, the evidence was admitted, and the defendant excepted to the ruling. We are unable to see upon what ground this evidence was competent. It was the declaration of a bankrupt in a proceeding in which it does not appear that this defendant was a party. As to this defendant the evidence would seem clearly to be hearsay and inadmissible."

§ 1748. Appraisal in Bankruptcy Inadmissible against Transferee.—The appraisal in bankruptcy is inadmissible against the transferee.⁴⁶

§ 1749. Declarations of Transferrer after Transfer.—It is a query whether the declarations of the alleged fraudulent transferrer made after the transfer may be admitted.

Compare, *In re Foster*, 11 A. B. R. 133, 126 Fed. 1014 (D. C. Pa.): "It may, perhaps, be true that declarations concerning the financial relation between Frank and himself, although made after the deed was delivered, are evidence in this issue between the bankrupt and the petitioning creditors. Upon this point the referee cited *Johnson v. Wald*, 2 Am. B. R. 84; but an examination of the report will show that it has no value as an authority. Evidence of similar declarations was no doubt received at the trial of that case, but there was

42. *Halbert v. Pranke*, 11 A. B. R. 620 (Sup. Ct. Minn.); *In re Elletson Co.*, 23 A. B. R. 530, 174 Fed. 859 (D. C. W. Va.); *Grinstead v. Union, etc., Co.*, 27 A. B. R. 123, 190 Fed. 546 (C. C. A. Wash.); instance, *Bean v. Orr*, 25 A. B. R. 400, 182 Fed. 599 (C. C. A. Ga.), reversing 24 A. B. R. 434.

43. *Horne-Gaylord Co. v. Miller & Bennett*, 17 A. B. R. 257, 147 Fed. 295 (D. C. W. Va.), which case is not authority, however, as to the right to bring the action in the bankruptcy court. *Underleak v. Scott*, 28 A. B. R. 926 (Sup. Ct. Minn.).

Judicial Cognizance of Records of Bankruptcy Court.—None in United States Circuit Court. *McDonald v. Clearwater Ry. Co.*, 21 A. B. R. 182, 164 Fed. 1007 (U. S. C. C. Idaho).

44. *Halbert v. Pranke*, 11 A. B. R. 620 (Sup. Ct. Minn.); *Hackney v. Raymond Bros. Clark Co.*, 10 A. B. R. 213 (Sup. Ct. Neb.); contra, *In re Docker-*

Foster Co., 10 A. B. R. 584 (D. C. Penn.). Also, ante, § 494. Compare, *obiter*, *Mattley v. Wolfe*, 23 A. B. R. 673, 175 Fed. 619 (D. C. Neb.), reversed, on other points, by *Mattley v. Giesler*, 26 A. B. R. 116, 187 Fed. 970 (C. C. A. Neb.), quoted at §§ 1379, 1382½, 1383; *Grant v. National Bank of Auburn*, 28 A. B. R. 712, 197 Fed. 581 (D. C. N. Y.). Contra, *Credit Men v. Furniture Co.*, 26 A. B. R. 867 (Utah).

45. *Breckons v. Snyder*, 15 A. B. R. 112, 211 Penn. St. 176; ante, § 1553. Contra, instance (though point not expressly passed upon), *Collett v. Bronx Nat'l Bk.*, 29 A. B. R. 454, 200 Fed. 111 (D. C. N. Y.); contra, impliedly, *In re Schoenfeld*, 27 A. B. R. 64, 190 Fed. 53 (D. C. W. Va.).

46. See, on analogous principle, cases cited in preceding paragraph, § 1747. Contra, *In re Docker-Foster Co.*, 10 A. B. R. 584 (D. C. Pa.).

no dispute concerning the fact that the vendee was a creditor, and the declarations were received without objection. In the Circuit Court of Appeals only one question was raised, and that concerned a different matter. But even if such declarations are evidence in an issue like this, the value of the testimony is evidently not great, and it certainly should be scanned with much care, especially since it stands alone without corroborating testimony. A peculiar result of sustaining the referee's finding might be, that in a suit by the trustee in bankruptcy against Frank the bankrupt's declarations made after the transfer could not be heard to affect his vendee's title, unless, perhaps, collusion were first shown (*Grimes Co. v. Malcom*, 164 U. S. 490; *Padgett v. Lawrence*, 40 Am. Dec. 232, note, and *Horton v. Smith*, 42 Am. Dec. 632) and we should have the anomaly of a cloud upon the vendee's title that depended solely upon evidence that could not be heard."

§ 1750. Failure to Produce Important Evidence, Presumption of Fraud.—Failure to produce important books or witnesses in a party's control raises a presumption that the evidence would be unfavorable to the party.⁴⁷

§ 1750¹/₂. Badges of Fraud and Latitude of Evidence.—The badges of fraud are to be considered together, for facts considered separately may be entirely insufficient to establish fraud, whilst considered together they may form an incontestible chain of proof of it.⁴⁸

Houck v. Christy, 18 A. B. R. 330, 152 Fed. 612 (C. C. A. Kans.): "Moreover, we think the evidence before recited brings the case well within the rule that badges of fraud, altogether inconclusive if separately considered, may, by their number and joint operation, especially when corroborated by moral coincidences, be sufficient to constitute conclusive proof of fraudulent intent on the part of both vendor and vendee."

And great latitude should be allowed in the admission of evidence, for questions of fraud can scarcely ever be proved by direct evidence.⁴⁹

In *re Luber*, 18 A. B. R. 476, 152 Fed. 492 (D. C. Pa.): "In the investigation of questions of fraud, as a rule, great latitude is allowed in the admission of evidence, in order that the jury may be able to determine from all the circumstances whether the transaction was fraudulent or not. Questions of fraud can scarcely ever be proved by direct evidence, hence the necessity for the admission of all the circumstances fairly connected with the transaction."

§ 1750³/₄. Possession as Prima Facie Proof of Ownership.—Possession of personal property draws with it the presumption of ownership.⁵⁰

§ 1751. Existence of Other Creditors at Time of Transfer, to Be Shown, unless.—It must appear that other creditors, or another creditor,

47. *Murray v. Joseph*, 16 A. B. R. 704 (D. C. N. Y.); *Nat'l Bk. v. Hobbs*, 9 A. B. R. 190 (U. S. C. C. Ga.); In *re Kellogg*, 7 A. B. R. 624, 113 Fed. 120 (D. C. N. Y.); instance, *Ott v. Doroshov*, 17 A. B. R. 417, 147 Fed. 762 (D. C. N. J.); instance, analogously (summary order on bankrupt), *Moody v. Cole*, 17 A. B. R. 825, 148 Fed. 295 (D. C. Me.).

48. In *re Larkins*, 21 A. B. R. 711, 168 Fed. 100 (D. C. N. Y.).

49. In *re Larkin*, 21 A. B. R. 711, 168 Fed. 100 (D. C. N. Y.).

50. In *re Diamond*, 19 A. B. R. 811, 158 Fed. 370 (D. C. Ala.); In *re Mayer*, 19 A. B. R. 480, 156 Fed. 432, 157 Fed. 836 (D. C. Pa.), quoted at § 554¹/₂.

existed at the date of the transfer complained of, than simply the ones or one to whom the transfer was made. Subsequent creditors cannot complain unless it is shown a scheme existed to defraud future creditors.⁵¹ But if the transfer were made in pursuance of a scheme to defraud subsequent creditors, it may be avoided.⁵²

§ 1751½. **Election of Remedies.**—It has been held that where a trustee, knowing the facts, has procured an order on the bankrupt for a surrender of the proceeds of an alleged fraudulent transfer still in his hands, the trustee will be held to have elected to affirm the transfer, in a subsequent suit against the alleged fraudulent transferee.

Thomas v. Sugerman, 19 A. B. R. 509, 157 Fed. 669 (C. C. A. N. Y.): "If the complainant was entitled to set the transfer aside as fraudulent, he could have recovered the account from Sugerman, but would have had to return to him the price or any part of it paid to the bankrupt which the complainant had received. This is because the right of the creditors was simply to be made whole. For the same reason, he would not have had to credit Sugerman with anything paid by Sugerman to the bankrupt which he, the complainant, had not actually received from the bankrupt. Of course, if the trustee had found the \$30,000 in the bankrupt's deposit box and taken it into his possession, or if the bankrupt had voluntarily paid the sum to him, the mere receipt of the money would not amount to an election by the trustee to affirm the transfer. But that is not the case. The trustee here, with a full knowledge of all the facts alleged in a formal proceeding that the bankrupt had in his possession and was concealing money, and by that proceeding he has, so to speak, created a fund. Nor can we adopt the appellant's theory that in this proceeding the trustee was merely seeking to get in the bankrupt's estate in order to determine, after it was in his hands, whether to affirm or to repudiate the transfer to Sugerman. The papers and proceedings show nothing of the kind, but, on the contrary, that he was seeking to get the money as a part of the bankrupt's estate to be distributed among the creditors. The case presents an election between inconsistent rights. It makes no difference that the defendant Sugerman was not a party to the proceeding in which the complainant charged the bankrupt with the money paid for the accounts transferred by him, or that the complainant actually recovered nothing in that proceeding. This act confirmed the title to those accounts in Sugerman." But see, dissenting opinion in same case. * * * "It is conceded that if the bankrupt had kept the \$30,000 in a private safe in some deposit company, and, upon learning of the appointment of the trustee, had delivered it to the latter, receipt of it would not constitute an election, and I cannot see how the situation is changed by the circumstances that the bankrupt delivers it in obedience to an order to show cause, or turns over only part of it because he has squandered the remainder. It would seem to be a disastrous rule to apply that, whenever a trustee insists that a bankrupt shall turn over all the property in his possession, he thereby ratifies by election all sorts of transactions which the bankrupt may have had with the persons from whom he got the prop-

51. *Brake v. Collison*, 11 A. B. R. 797, 129 Fed. 196 (C. C. A. Fla., affirming *In re Collison*, 12 A. B. R. 344, 130 Fed. 987).

52. *Beasley v. Coggins*, 12 A. B. R. 555; S. C., 57 So. Rep. 213, 48 Fla. 215.

Obiter, *In re Collison*, 12 A. B. R. 344, 130 Fed. 987 (D. C. Fla.).

Instance held not in fraud of subsequent creditors, *In re Foss*, 17 A. B. R. 439, 147 Fed. 790 (D. C. Mo.).

erty; and I am not satisfied that the authorities cited require such an extension of the doctrine of election."

§ 1752. **Collateral Attack on Collusive Receiverships.**—No collateral attack on a state court receivership, as being fraudulent or collusive, will be permitted by the bankruptcy trustee where he might have raised the question in the state court.⁵³

§ 1753. **Suing in United States District Court, Suit Follows Usual Course.**—Where the plenary action is brought in the United States District Court, it follows the usual course of procedure therein.⁵⁴

Westall v. Avery, 22 A. B. R. 673, 171 Fed. 626 (C. C. A. N. C.): "But independent of this, it is also well settled that a proceeding instituted by a bankrupt's trustee to set aside fraudulent conveyances or illegal preferences is not a proceeding in bankruptcy but, while ancillary to such proceeding and authorized by the Bankruptcy Act to be instituted in either the Federal District Court or in a State court of competent jurisdiction, it must be governed, so far as pleading and practice are concerned, by the laws and rules of the court wherein it is instituted. * * * And further, it is to be borne in mind, that the equity practice of the Federal courts is independent of, and unaffected by State laws as to procedure in State courts. *Payne v. Hook*, 7 Wall. 430, 19 L. Ed. 261; *Scott v. Neely*, 140 U. S. 106, 35 L. Ed. 358. In Federal courts the rules of the High Court of Chancery in England are recognized as 'the common law of chancery' and an authoritative exposition of the principles, rules and usages belonging to courts of equity except so far as they may be modified by Federal statute and by rules promulgated by the Supreme Court. *Penn'a v. Wheeling &c. Bridge Co.*, 13 How. 563, 14 L. Ed. 249. Finally it is to be observed, that Federal courts, both when exercising general jurisdiction and also when exercising the special one conferred by the Bankruptcy Act in this particular, require suits to set aside deeds and contracts as fraudulent to be instituted in equity."

Thus, whether the reference of issues to a person constitute him, under the circumstances, a special master or an arbitrator, is to be decided by the rules of the forum.⁵⁵

§ 1753¼. **Whether, Where No Jury, Court to Take Evidence Considered Incompetent, etc.**—It has been held to be the duty of the court, where no jury is called, to take all the evidence, even if considered by the

53. *Frazier v. Southern Loan & Trust Co.*, 3 A. B. R. 710, 99 Fed. 707 (C. C. A. N. Car.).

54. *Kraver v. Abrahams*, 29 A. B. R. 365, 203 Fed. 782 (D. C. Pa.); *Lovell v. Latham & Co.*, 26 A. B. R. 599, 186 Fed. 602 (C. C. Ala.), as to availability of cross bill. Thus, the time limit for appeal in such cases is not ten days, as it would be under § 25; but is governed by the provisions of the act creating the Circuit Courts of Appeal. *Boonville Nat'l Bk. v. Blakey*, 6 A. B. R. 13 (C. C. A. Ind.).

The rule that the bankruptcy court has no terms and that its orders may be vacated on good cause and proper application even after expiration of the current term of the District Court is hardly applicable to plenary actions for the recovery of property. It is confined to bankruptcy proceedings proper. Compare broad statement of the rule in *In re Ives*, 7 A. B. R. 692, 113 Fed. 911 (C. C. A. Mich.).

55. *Westall v. Avery*, 22 A. B. R. 673, 171 Fed. 626 (C. C. A. N. Car.).

court to be incompetent, immaterial, or otherwise inadmissible, in order that a reviewing court may not be obliged to remand the case for admission of the rejected evidence, exception being made, however, of cases where the testimony is privileged or the evidence so clearly incompetent or irrelevant as that its production or admission would amount to abuse of process.

Missouri Elec. Co. v. Hamilton-Brown Co., 21 A. B. R. 270, 165 Fed. 283 (C. C. A. Mo.): "A proceeding in bankruptcy is a proceeding in equity, and it is the duty of examiners, masters, referees, and the court, when taking evidence in controversies therein in the absence of a jury, to take, record, and in case of an appeal, to return to the reviewing court, all the evidence offered by either party, that which they hold to be incompetent or immaterial as well as that which they deem competent and relevant, to the end that, if the appellate court is of the opinion that evidence rejected should have been received, it may consider it, render a final decree, and thus conclude the litigation without remanding the suit to procure the rejected evidence. From this rule evidence plainly privileged, the testimony of privileged witnesses and evidence which clearly and affirmatively appears to be so incompetent, irrelevant, and immaterial that it would be an abuse of the process or power of the court to compel its production or permit its introduction, are excepted."

§ 1753¹/₂. **But Bankruptcy Court Has Full Equity Powers.**—The bankruptcy court, in such suits, exercises full equity powers and is not confined to the mere avoidance of the transfer and decree for the recovery of the property, but may protect and enforce rights of the parties in other particulars.⁵⁶ And in proceedings in equity instituted by the trustee the rules of equity practice established by the United States Supreme Court are to be followed as nearly as may be.⁵⁷

§ 1753³/₄. **Statutory Prerequisites to "Maintaining Suits."**—State statutes prohibiting parties from maintaining or instituting suit until they have complied with certain registry or deposit requirements, etc., have no applicability to suits in the federal courts; the federal court may accept the substantive rights of the parties as it finds them under the State statutes; but will itself determine what shall be the prerequisites to the maintenance of suits in its own forum.⁵⁸

In re Dunlop, 19 A. B. R. 361, 156 Fed. 545 (C. C. A. Minn.): "This statute has received the consideration of the highest judicial tribunal of Minnesota, and it has held that such a foreign corporation cannot maintain an action in the courts of that State to recover the purchase price of goods sold by it in the transaction of business in the State without complying with the conditions of this statute * * * or for the recovery of moneys collected for it by its agent on account of the sale of its goods and evidenced by the agent's note. * * * The reason which induced the Supreme Court of Minnesota to reach these conclusions, as we understand its opinions, was not that the con-

56. *Allen v. McMannes*, 19 A. B. R. 276, 156 Fed. 615 (D. C. Wis.).

57. Gen. Ord. No. 37.

58. But compare, apparently contra, in principle, *In re Montello Brick*

Works, 20 A. B. R. 855, 163 Fed. 621 (D. C. Pa.); compare, *In re Duplex Radiator Co.*, 15 A. B. R. 324, 142 Fed. 906 (D. C. N. Y.). See also, ante, § 803¹/₂; compare, ante, § 35.

tracts upon which the actions were brought were void because violative of the statute, but it was that the State had the undoubted right to exclude foreign corporations which would not submit themselves to the jurisdiction of the courts of the State from the privilege of enforcing rights and litigating controversies in those courts, and that it had clearly done so in the cases which have been cited. But the provision of the State statute which forbids the maintenance of suits in the courts of that State was not intended to apply to, and it does not affect, suits and proceedings in the Federal courts. A State is without power to prohibit or condition the exercise by a foreign corporation of its right to institute and defend its suits in the national courts and to invoke their independent judgment upon its controversies in the cases and in the manner prescribed by the Constitution and laws of the United States, which are the supreme law of the land."

But in Alabama the statute goes further than merely to prohibit the maintenance of the suit: it makes the contract itself illegal and void, so that the trustee of a foreign corporation which was doing business there without compliance with the state statute cannot maintain a suit on the contract nor on quantum meruit even in the federal court, the contract furthermore not being in interstate commerce.⁵⁹

§ 1754. Allegation of Diverse Citizenship Not Requisite.—Allegation of diverse citizenship is not necessary, except where the action brought in the United States District Court is not one for the recovery of property transferred by the bankrupt preferentially or in fraud of his creditors or for the recovery of its proceeds. The jurisdiction depends upon its being a bankruptcy controversy cognizable under the Act, not upon diversity of citizenship.⁶⁰ But the facts constituting it such a cognizable controversy must be pleaded and proved.⁶¹

§ 1755. Service on Nonresidents When Suit in United States District Court.—Service may be had over nonresidents interested in the property under U. S. Rev. Stat., § 738.⁶²

59. *Thomas v. [Birmingham] Railway Co.*, 28 A. B. R. 152, 195 Fed. 340 (D. C. Ala.).

60. *Wright v. Skinner*, 14 A. B. R. 500, 136 Fed. 694 (D. C. N. Y.). See § 1686.

61. Compare, analogously, to same effect, § 1730½.

62. *Horskins v. Sanderson*, 13 A. B. R. 101, 132 Fed. 415 (D. C. Vt.).

Costs and Expenses in Suits Brought by Receivers and Trustees in Bankruptcy against Third Parties.—If the court decides that the property was wrongfully seized, then no part of the costs nor any part of the expenses of its care can be charged against the successful party. *Beach v. Macon Grocery Co.*, 11 A. B. R. 104, 125 Fed. 513 (C. C. A. Ga.).

The bankruptcy court may order the trustee or receiver to comply with

the judgment of the court to pay costs where the suit is unsuccessful, impliedly, *In re Howard*, 12 A. B. R. 462, 130 Fed. 1004 (D. C. Calif.). But only where there are funds sufficient: otherwise execution or action is the only remedy.

In re Howard, 12 A. B. R. 462, 130 Fed. 1004 (D. C. Calif.): "The judgment of the Circuit Court, in so far as it relates to costs, can only be enforced by execution or by action. It cannot be enforced in this summary proceeding, as it is conceded that there are not now, and never have been, any funds in the hands of the trustee belonging to the petitioner or to the estate of the bankrupt with which to satisfy the same."

Stakeholder.—In one case it was held that where a mere stakeholder who claimed interest in the fund or

§ 1756. Security for Costs and Injunction Bond When Suit in United States District Court.—Security for costs will not be required of receivers or trustees suing in independent actions in the United States District Courts, at least in the same jurisdiction wherein appointed, if there are sufficient assets in the estate, unless the suits are not brought in good faith.⁶³ But such security perhaps may be required where brought by a nonresident trustee in the United States District Court on the ground of diversity of citizenship.⁶⁴

§ 1757. Answering under Oath Requiring Testimony to Overcome.—If suit be in the United States District Court and the defendant answers under oath it will require the testimony of two witnesses or of one witness and corroborating circumstances to overcome the oath; if the answer under oath is waived, however, it will not so require.⁶⁵

§ 1758. If Suit in United States District Court, Party Not to Impeach Own Witness.—If the suit be brought in the United States District Court a party may not impeach his own witnesses and is bound by their testimony, except that he may show a mistake.⁶⁶

Compare, instance, *Entwisle v. Seidt*, 19 A. B. R. 185, 155 Fed. 864 (D. C. N. Y.): "The witnesses called on behalf of the complainants are the defendants, and the persons engaged as principals in the various transactions. Their examination was conducted apparently on the theory that they were biased witnesses, to such an extent that the complainant would not be bound by the statements made, and the direct examination is in almost all cases in reality cross-examination. But the complainant has presented no proofs showing any of the facts alleged, outside of the testimony of these witnesses produced by himself, and aside from the general situation there is nothing brought out to show bias nor fraudulent motives on the part of the parties to the transaction. The attorneys for all the parties have so violated the rules of evidence that the most of the testifying has been done by the attorneys, apparently without objection, and it is impossible from a reading of the testimony as transcribed to form an opinion as to whether the witnesses were telling the truth, or whether they were following the lead of the testimony put into their mouths by the questions of the attorneys. On the whole testimony, it would appear that the complainant is bound by the statements of his own witnesses, and in every instance these statements show a valid consideration and an actual transfer of property. There is no extraneous or disinterested testimony to prove the contrary. As to the mortgage in question the testimony shows plainly that the transaction occurred exactly as claimed by the bankrupt. It appears that the defendant Cohen, assignee of the mortgage, is a brother-

profits issued and the adverse claimant intervened or was made party, the stakeholder might be relieved from costs, and (if proper according to State law), might even be allowed counsel fees. *Caten v. Eagle Ass'n*, 23 A. B. R. 130, 177 Fed. 996 (D. C. Pa.).

^{63.} *In re Barrett*, 12 A. B. R. 626, 132 Fed. 362 (D. C. Tenn.); *In re Baird*, 17 A. B. R. 448, 112 Fed. 960 (D. C.

Pa.). As to security for costs when suit in State court, see post, § 1760.

^{64.} Impliedly, *Osborne v. Pa. Ry. Co.*, 20 A. B. R. 277, 159 Fed. 301 (U. S. C. C. Pa.).

^{65.} *Jacobs v. Van Sickle*, 11 A. B. R. 479, 127 Fed. 62 (C. C. A. N. J.); *Dravo v. Fabel*, 132 U. S. 489.

^{66.} *Jacobs v. Van Sickle*, 11 A. B. R. 479, 127 Fed. 62 (C. C. A. N. J.); *Dravo v. Fabel*, 132 U. S. 489.

in-law of the bankrupt, and the apparent object of the action, as far as the mortgage is concerned, is to show that Cohen purchased a valid mortgage for the benefit of the bankrupt, and, inferentially, with funds supplied by the bankrupt. But no evidence whatever is furnished as to these surmises, and no examination of the defendant Cohen, as to the source of the funds with which he purchased the mortgage, and no evidence of other witnesses as to where the money used by him was obtained, is offered. The complainant's case as to this mortgage rests merely upon the contradictory statements and the rather lame explanations of motive on the part of the defendant Cohen, who, nevertheless, is shown by the testimony to have actually purchased for a valid consideration the assignment of the mortgage in question."

§ 1759. State Statutes Permitting Cross-Examination of Adverse Party, etc., Not Followed.—State statutes permitting the cross-examination of the adverse party and providing that his answers shall not conclude the party so examining but may be rebutted, are not applicable to federal equity practice.⁶⁷

§ 1759½. No Demurrer to Answer in Federal Court.—If the suit be brought in the federal court no demurrer to the answer will lie; but such a demurrer may be treated as an application to set the cause down for hearing on bill and answer, or as an exception to the answer for impertinence or for failure to answer fully.⁶⁸

Vitzthum v. Large, 20 A. B. R. 666, 162 Fed. 685 (D. C. Iowa): "This proceeding is quite irregular, and if stipulations like these are to be observed it will enable the parties to a suit in equity to abrogate entirely the equity rules, and require the court to proceed in equity causes as in actions at law. While the equity rules should not be so strictly enforced as to do injustice to either party, a reasonable adherence to them is necessary to orderly procedure, and to enable the court to bring the parties to final issues upon the merits. Under the practice as prescribed by the State statute, which counsel desire to have observed, a demurrer admits the allegations of the pleading demurred to for the purpose of the demurrer only, and if the demurrer is overruled, and the party demurring shall answer or reply, which he may do, the ruling on the demurrer shall not be considered as an adjudication of any question raised by the demurrer, and no pleading shall be held sufficient because of a failure to demur thereto. Code Iowa 1897, §§ 3564, 3565. Such a practice is so at variance with the equity procedure in the national courts that parties should not be permitted to introduce it into those courts to the exclusion of the procedure prescribed by the equity rules. A demurrer to an answer in equity

67. *Jacobs v. Van Sickle*, 11 A. B. R. 479, 127 Fed. 62 (C. C. A. N. J.). Also, see *Dravo v. Fabel*, 132 U. S. 489.

But **Communications Privileged by State Law, Privileged in Federal Courts.**—Communications privileged under State law have been held to be privileged in the U. S. District Court. Thus, where a husband and wife are prohibited by State statute from testifying against each other the schedules in bankruptcy of one have been held inadmissible in a fraudulent conveyance

suit against the other. *Halbert v. Pranke*, 11 A. B. R. 621, 91 Minn. 204.

Impeaching Credibility of One's Own Witness.—*Greenhall v. Carnegie Trust Co.*, 25 A. B. R. 300, 180 Fed. 812 (D. C. N. Y.); *In re Calvi*, 26 A. B. R. 206, 185 Fed. 642 (D. C. N. Y.).

Compare analogous propositions as to rejecting incredible, though uncontradicted, testimony, ante, §§ 554, 555, 852, and post, § 2650.

68. See ante, *Goldman v. Smith*, 1 A. B. R. 266, 93 Fed. 182 (D. C. Ky.).

is unknown to the equity practice, and the only way of testing the sufficiency of an answer in equity as a defense to the bill is to set the cause down for hearing upon bill and answer. *Banks v. Manchester*, 128 U. S. 224-250, * * * *In re Sanford Fork & Tool Co.*, 160 U. S. 247-257, * * *; 1 *Bates*, Fed. Eq., sec. 216. A formal demurrer filed to an answer may, however, be treated by the court, in the absence of objections to so doing, as an application to set the cause down for hearing upon bill and answer, or as an exception to the answer for impertinence, or for failure to answer fully according as its contents may present the one or the other of these questions."

§ 1760. Where Trustee Sues in State Court, Suit Follows Usual Course and Parties Have Usual Rights, There.—Where the trustee resorts to the state court to recover fraudulently conveyed property or property otherwise recoverable, he is entitled to all remedies and all relief that would be afforded any other party litigant under the same facts.⁶⁹ Thus, where the state law permits a simple contract creditor to maintain a suit to set aside a fraudulent conveyance, the trustee has the same right⁷⁰ and is bound to make proof in accordance with the state law.

Impliedly, *Miller v. Acid & Fertilizer Co.*, 21 A. B. R. 416, 211 U. S. 496: "Undoubtedly, the trustee, in prosecuting the suit to judgment, was obliged to prove to the existence of the facts which were essential under the State laws, since, to hold otherwise would be but to decide that he could recover without proof of his right to do so."

And the rules of procedure of the state court will control.⁷¹ So, also, as to the form of action.⁷² Thus, also, in New York it is held, in suits brought by trustees in the state courts, that the rule that unfiled chattel mortgages are "void as against creditors" does not require the existence of levying creditors, but that, if judgment creditors exist, it is enough.⁷³ Such does not, however, seem to be the rule where the suit is brought in the federal court there.

Thus, also, the trustee is bound to give security for costs where such security would be required of others,⁷⁴ and the trustee may be ordered to pay the taxable costs of an action wherein he has been defeated,⁷⁵ and the alleged fraudulent transferee is entitled to urge all defenses against the trustee.

So, the State law will control as to the right of trial by jury.⁷⁶

69. *Shelton v. Parker*, 11 A. B. R. 152, 66 Neb. 610. Compare, "Directing Verdict on Question of Insolvency," § 1770 3/5.

70. *Andrews v. Mather*, 9 A. B. R. 300, 134 Ala. 358; *Grunsfeld Bros. v. Brownell*, 11 A. B. R. 601 (Sup. Ct. New Mexico).

71. *Westall v. Avery*, 22 A. B. R. 673, 171 Fed. 626 (C. C. A. N. Car.).

72. *Reber v. Ellis Bros.*, 25 A. B. R. 567, 185 Fed. 313 (D. C. Pa.).

73. *Gove v. Morton Trust Co.*, 12 A. B. R. 297, 96 App. Div. 177 (Sup. Ct. N. Y. App. Div.). Compare, *In re*

Beede, 11 A. B. R. 387, 120 Fed. 853 (D. C. N. Y.); *Skilton v. Codington*, 15 A. B. R. 819, 185 N. Y. 80.

74. *Joseph v. Raff*, 9 A. B. R. 227 (App. Div. Sup. Ct. N. Y.).

That he need not give security, in New York, or at any rate that no ex parte order therefor will lie, see *Ryker v. Gwynne*, 21 A. B. R. 95 (Sup. Ct. N. Y. Sp. Term); *Kronheld v. Leibman*, 79 N. Y. Supp. 1083.

75. *In re Havens*, 25 A. B. R. 116, 182 Fed. 367 (D. C. N. Y.).

76. *Allen v. Gray*, 25 A. B. R. 423 (N. Y.).

A suit to set aside a fraudulent transfer being, under state rules, in equity, it is proper to deny a jury trial.⁷⁷ So, also, the rules of the state court will prevail as to directing a verdict when the facts are undisputed.⁷⁸

SUBDIVISION "C."

PLEADINGS AND PRACTICE IN PROCEEDINGS TO SET ASIDE AND RECOVER PREFERENCES.

§ 1761. **Representative Capacity of Trustee to Be Alleged.**—The representative capacity of the trustee of course must be alleged. But the entire pleading may be taken to ascertain the allegation.⁷⁹ Also, whether the suit is brought in a state court⁸⁰ or in the federal court the trustee's appointment should be proved.

§ 1761½. **Pleading Claims of Creditors and Inadequacy of Assets.**—The trustee need not plead, nor prove, specifically, that claims against the bankrupt have been filed and allowed, although it is probably necessary to plead and prove in some form that the bankrupt is indebted to general creditors who may share in the preference recovered.⁸¹

Gering v. Leyda, 26 A. B. R. 137, 186 Fed. 110 (C. C. A. Neb.): "It is contended in behalf of plaintiffs in error that the trustee's petition failed to state a cause of action entitling him to recover a preference because it is not averred therein that at the time of the commencement of the action the claims of any creditors had been proved and allowed against the estate of the bankrupt. In our opinion it was not necessary for the trustee to allege and prove that claims of creditors had been filed and allowed against the estate of the bankrupt prior to the commencement of the suit. The trustee's petition alleged that at the time of the transfer in question the bankrupt was hopelessly insolvent and that his indebtedness amounted to over \$24,000 and that the only unexempt property then owned by him was the stock of merchandise conveyed to plaintiffs in error, and we are of opinion that these allegations sufficiently charged that at the time of the transfer complained of the bankrupt was indebted to general creditors, who were not secured, and who were entitled to share in the preference recovered. We think the trustee's petition stated a good cause of action, for the recovery of a preference. *Swartz v. Fourth Nat'l Bank* (C. C. A. 8th Cir.), 8 A. B. R. 673, 117 Fed. 1; *Coder v. McPherson*, 18 A. B. R. 523, 152 Fed. 951 (C. C. A. 8th Cir.); *Wright v. Skinner Mfg. Co.* (C. C. A. 2nd Cir.), 20 A. B. R. 527, 162 Fed. 315; *Tumlin v. Bryan* (C. C. A. 5th Cir.),

77. *Allen v. Gray*, 24 A. B. R. 642, 105 N. Y. App. Div. 643.

78. *Shale v. Farmers' Bank*, 25 A. B. R. 888, 82 Kan. 649.

79. *Newland v. Zedikow*, 11 A. B. R. 770, 80 N. Y. Supp. 378.

Miscellaneous decisions: *Richter v. Nimmo*, 6 A. B. R. 680, 71 N. Y. Supp. 501; *Chism v. Bank*, 5 A. B. R. 56, 77 Miss. 599; *Lesser v. Bradford Realty Co.*, 17 A. B. R. 524, 116 App. Div. 212 (N. Y.).

Defense that title had never passed because of misrepresentation, and that the sale had been rescinded, should aver intent to deceive and actual reliance on the misstatements. *Lumber Co. v. Taylor*, 14 A. B. R. 231, 137 Fed. 321 (C. C. A. Penn.).

80. *McKey v. Smith*, 28 A. B. R. 864 255 Ill. 465.

81. Compare ante, §§ 1731, 1736, et seq.

21 A. B. R. 319, 165 Fed. 166; *In re Leech* (C. C. A. 6th Cir.), 22 A. B. R. 599, 171 Fed. 622.

"(1) It is not necessary in such a case for the trustee to plead and prove that claims against the bankrupt have been filed and allowed; (2) it is necessary for him to plead and prove that the bankrupt is indebted to general creditors who may share in the preference recovered (3) the complaint sufficiently alleges that the bankrupt was indebted in an amount very much in excess of the claims secured by the preference so that it is sufficient in this regard; (4) the defendants below by objecting to the proof of indebtedness of the bankrupt on the ground that such proof was immaterial and obtaining a ruling sustaining this objection, estopped themselves from claiming that evidence of such indebtedness was requisite to sustain the trustee's cause of action, notwithstanding this ruling, sufficient evidence crept into the case to constitute substantial evidence of indebtedness of the bankrupt to general creditors not secured."

It has been held that the petition must allege an insufficiency of assets in the trustee's hands.⁸³ Where proof of insolvency at the time of the alleged preference is made at the trial, such proof is *prima facie* proof that insolvency existed at the time of the filing of the bankruptcy petition.⁸⁴

§ 1762. **Each Element of Preference to Be Alleged and Proved.**—Each element of the preference must be alleged and proved.⁸⁵

§ 1763. **Insolvency at Time of Transfer.**—Thus, the petition to recover the preference must allege that the bankrupt was, at the time, insolvent,⁸⁶ and an allegation that he was in failing circumstances and unable to meet his debts is insufficient on demurrer, such allegation not being the equivalent of insolvency.⁸⁷ But the pleader should not allege the amount of the indebtedness, nor the value of the debtor's assets.⁸⁸

§ 1763 1/10. **Admissibility of Schedules, Inventory and Appraisal, and General Examination of the Bankrupt.**—We have previously seen that the schedules filed by the bankrupt are inadmissible against the alleged preferred creditor to prove the bankrupt's insolvency, being merely the admissions of an assignor after he has parted with his interest to the alleged preferred creditor;⁸⁹ we have also discussed the admissibil-

83. *Lesser v. Bradford Realty Co.*, 15 A. B. R. 123, 47 N. Y. Misc. 463.

84. **Estoppel of Defendants by Obtaining Favorable Ruling Excluding Evidence of Indebtedness.**—*Gering v. Leyda*, 26 A. B. R. 137, 186 Fed. 110 (C. C. A. Neb.).

85. *In re Leech*, 22 A. B. R. 599, 171 Fed. 622 (C. C. A. Ky.), quoted at § 1277; *In re Carlile*, 29 A. B. R. 333, 199 Fed. 612 (D. C. N. Car.); *Utah Ass'n of Credit Men v. Boyle Fur. Co.*, 26 A. B. R. 867 (Sup. Ct. Utah); *Rodolf v. First Nat. Bank*, 28 A. B. R. 897 (Sup.

Ct. Okla.); *McKey v. Smith*, 28 A. B. R. 864 (Sup. Ct. Ill.).

Stating Facts Both as to Fraudulent Transfer and as to Preference.—Compare *Carey v. Donohue*, 31 A. B. R. 210, 209 Fed. 328 (C. C. A. Ohio).

86. *In re Leech*, 22 A. B. R. 599, 171 Fed. 622 (C. C. A. Ky.), quoted ante at § 1277.

87. *Martin v. Bigelow*, 7 A. B. R. 218 (Sup. Ct. N. Y.).

88. *Crooks v. People's Bk.*, 3 A. B. R. 243, 46 N. Y. App. Div. 335.

89. See ante, § 1356.

ity of the inventory and appraisal taken in the bankruptcy court.⁹⁰ We have seen, further, that a general examination of the bankrupt is competent as an admission in subsequent litigation against the bankrupt himself but that it is not admissible against any other party.⁹¹

§ 1763 2 10. **Admissibility of Bankrupt's Books.**—Books of the bankrupt are competent evidence on the question of his insolvency.⁹² Of course, their competency is not on the basis of their being admissions, but rather on their being contemporaneous memoranda.

§ 1763 3 10. **Whether Sale by Receiver in State Court or by Trustee in Bankruptcy Competent.**—Whether sales by a receiver in the state court or by the trustee in the bankruptcy court are evidence of the value of the assets, in a suit between the trustee and a preferred creditor, is discussed ante, in § 1358.

§ 1763 4/10. **Referee's Allowance of Claims, Whether Admissible.**—Whether the referee's allowance of claims are admissible as to the liabilities of the bankrupt is discussed ante, § 1359; also, post, § 1771.

§ 1763 5/10. **Return of Execution Unsatisfied, Whether Prima Facie Proof of Insolvency.**—It has been held that the return of an execution unsatisfied in whole or in part is not even prima facie proof of insolvency.⁹³

§ 1764. **Reasonable Cause of Belief.**—It must allege that the creditor had reasonable cause to believe that enforcement of the transfer would effect a preference, and such fact must be alleged definitely and certainly.⁹⁴

Carey v. Donohue, 31 A. B. R. 210, 209 Fed. 328 (C. C. A. Ohio): "It is true, as counsel claim, that this court has held that in a suit to set aside a voidable preference, it is necessary to allege that the person receiving the preference had reason to believe that it was intended to give 'a preference forbidden by law.' In *re Leech*, 22 A. B. R. 599, 171 Fed. 625. While that decision was rendered before, and the present transaction occurred since, the amendment of 1910 to § 60 b, yet the element of reasonable belief of the creditor remains as a fact necessary in substance to allege."

90. See ante, § 1357.

91. See ante, § 1555.

92. See ante, § 1335.

93. See ante, § 1361.

94. *Johnson v. Anderson*, 11 A. B. R. 294 (Sup. Ct. Neb.); *Peck v. Cornell*, 8 A. B. R. 500 (Super. Ct. Pa.); *In re Blair*, 4 A. B. R. 220, 102 Fed. 987 (D. C. N. Y.).

It is not necessary also to allege that the creditor had reasonable grounds to believe the debtor was insolvent: belief of insolvency is included within belief of preferential intent. Compare, ante, § 1404. *Contra*, *Hicks v. Langhorst*, 6 A. B. R. 178 (Com. Pleas Ohio).

But it should not allege why the creditor had such reasonable cause, nor the evidence to demonstrate it. *Crooks v. People's Bk.*, 3 A. B. R. 244, 46 N. Y. App. Div. 335.

Obiter, *Carey v. Donohue*, 31 A. B. R. 210, 209 Fed. 328 (C. C. A. Ohio).

The test of sufficiency for submission to the jury is not to rest on assertions of lack of intent or belief but on inferences which may fairly be drawn from the facts in evidence. *Obiter* (creditor being exonerated), *Hamilton Bank v. Balcomb*, 24 A. B. R. 338, 177 Fed. 155 (C. C. A. Ills.).

However, on appeal from a decree in favor of the trustee, the failure of the petition to allege the existence of the reasonable cause for belief will only cause a reversal and remanding of the cause for the purpose of appropriate amendment and re-entry of the decree.⁹⁵

§ 1765. **Effect of Transfer to Give Greater Percentage of Debt.**—It must allege that the effect was to give the creditor, etc., a greater percentage of his claim than some other of the same class;⁹⁶ but it need not set forth facts showing why.⁹⁷ It need not, on the other hand, allege the legal conclusion if it does set forth the facts.⁹⁸

West v. Bank of Lahoma, 16 A. B. R. 733, 16 Okla. 508: "A petition by a trustee in bankruptcy against a creditor of the bankrupt to recover money alleged to constitute a preferential transfer, must, among other averments, show that, if the transfer is permitted to stand, the creditor will receive a greater percentage of its debt than other creditors of the same class, and, failing to show such state or facts, it is not error to sustain a demurrer to such petition."

§ 1766. **Antecedent Debt.**—It must also be alleged and proved that the transfer was to apply upon an antecedent debt.⁹⁹

§ 1767. **Facts, Not Evidence, nor Legal Conclusions, to Be Pleaded.**—The pleader is to state facts, not to demonstrate them nor allege the evidence of them.¹ And the legal conclusion that the transfer is voidable is not necessary when the facts pleaded show it to be voidable.²

§ 1768. **Burden of Proof of Each Element on Trustee.**—The burden of proof is on the trustee to prove each element of the preference.³

Tumlin v. Bryan, 21 A. B. R. 319, 165 Fed. 166 (C. C. A. Ga.): "The burden of proof is on the complainant, and, unless he shows by sufficient evidence the elements of a voidable preference, he is not entitled to recover. He must prove that the bankrupts (1) while insolvent, (2) within four months of the bankruptcy, (3) made a transfer of the property, e. g., a payment of money, (4) and that the creditor receiving the payment was thereby enabled to obtain a greater percentage of his debts than other creditors of the same class; and

95. *Carey v. Donohue*, 31 A. B. R. 210, 209 Fed. 328 (C. C. A. Ohio).

96. *Crooks v. People's Bk.*, 3 A. B. R. 243, 46 App. Div. N. Y. 335.

97. *Crooks v. People's Bk.*, 3 A. B. R. 243, 46 App. Div. N. Y. 335.

98. *Lesser v. Bradford Realty Co.*, 17 A. B. R. 526, 116 App. Div. 212 (N. Y.).

99. *Lesser v. Bradford Realty Co.*, 15 A. B. R. 123, 47 N. Y. Misc. 463 (N. Y. Sup. Ct., affirmed 17 A. B. R. 524).

Definition of "Antecedent Debt."—See ante, §§ 123, 1314.

1. *Crooks v. People's Bk.*, 3 A. B. R. 243, 46 App. Div. N. Y. 335.

2. *Lesser v. Bradford Realty Co.*, 17 A. B. R. 527, 116 App. Div. 212 (N. Y.).

3. As to insolvency, see *In re Chap-*

pell, 7 A. B. R. 608, 113 Fed. 545 (D. C. Va.). As to reasonable cause for belief, *In re Keith v. Gettysburg Nat'l Bk.*, 10 A. B. R. 762, 23 Penn. Super. Ct. 14.

See ante, §§ 775½, 1403½; *In re Pfaffinger* (arising, however, on objection to allowance of claim), 18 A. B. R. 570, 175 Fed. 259 (D. C. N. Y.), partially to same effect, *Allen v. Gray*, 21 A. B. R. 828 (N. Y. Sup. Ct.); *Getts v. Janesville Grocery Co.*, 21 A. B. R. 5, 163 Fed. 417 (D. C. Wis.); *Calhoun County Bank v. Cain*, 18 A. B. R. 509, 152 Fed. 983 (C. C. A. W. Va.); but compare, where transfer is to a relative, *In re Sanger*, 22 A. B. R. 145, 169 Fed. 722 (D. C. W. Va.).

it must also be proved, (5) that the person receiving the payment or to be benefited thereby, had reasonable cause to believe that it was thereby intended to give a preference."

§ 1769. Demand Not Requisite.—No allegation of demand is necessary, and no demand need be proved;⁴ for the beginning of the action is sufficient demand, even if the action be in trover.⁵ Demand is unnecessary where it would be useless.⁶

§ 1770. Nor Tender Back.—The trustee need not tender back any of the preference actually already received.⁷

§ 1770⅛. On Surrender, Creditor Entitled to Prove Claim for Share of Dividends.—After the transfer has been set aside, the creditor is entitled to prove his claim for sharing in dividends.⁸

§ 1770¼. Or, Dividends May Be Offset.—And if the suit be in the bankruptcy court wherein the estate is being administered, the decree may provide for applying the dividends on the amount ordered surrendered, the preferential transferrer being entitled to his dividend, in any event.

Page *v. Rogers*, 211 U. S. 581, 21 A. B. R. 496: "Now that this litigation has come to an end, and the defendant has been compelled to surrender the preference which he received, he is entitled to prove his claim and to receive a dividend on it upon an equality with other creditors. *Keppel v. Tiffin Sav. Bank*, 197 U. S. 356, 13 Am. B. R. 552, 49 L. Ed. 790, 25 Sup. Ct. Rep. 443. In view of the fact that this suit was brought in the bankruptcy court itself, and a final decree is to be entered by the judge of that court, it is entirely practicable to avoid the circuitous proceeding of compelling the defendant to pay into the bankruptcy court the full amount of the preference which he has received, and then to resort to the same court to obtain part of it back by way of dividend."

But if the suit be in another court it has been held that the preferred creditor may not offset but must surrender first and then prove his claim for dividends on the whole amount.⁹ However, even where the suit be thus in another court, it probably is the better rule that if the suit be in a court of equity the preferred creditor may still retain his prospective dividend, the court sometimes requiring the giving of a bond as a condition of such retention.¹⁰

§ 1770⅓. Amendment.—Amendments are permitted, under the or-

4. *Eau Claire Nat'l Bk. v. Jackman*, 17 A. B. R. 675, 204 U. S. 522 (affirming 125 Wis. 478); *Wright v. Skinner*, 14 A. B. R. 500, 136 Fed. 694 (D. C. N. Y.).

5. *Eau Claire Nat'l Bk. v. Jackman*, 17 A. B. R. 675, 204 U. S. 522.

6. *Utah Ass'n v. Boyle Furniture Co.*, 31 A. B. R. 488, 39 Utah 518.

7. *Stern, Falk & Co. v. Trust Co.*, 7 A. B. R. 305, 112 Fed. 501 (C. C. A. Ky.); *obiter, Drew v. Myers*, 22 A. B.

R. 656, 81 Neb. 750, quoted at § 1192.

8. See ante, § 772; *Templeton, Trustee, v. Kehler*, 23 A. B. R. 39, 173 Fed. 574 (D. C. Pa.); *Page v. Rogers*, 21 A. B. R. 496, 211 U. S. 581.

9. *Templeton v. Kehler*, 23 A. B. R. 39, 173 Fed. 574 (D. C. Pa.).

10. *Ommen, Trustee, v. Talcott*, 23 A. B. R. 807, 154 Fed. 528 (D. C. N. Y. partly reversed, on other grounds, S. C., 26 A. B. R. 689, 188 Fed. 401). See also; §§ 775, 1178, 1179½.

ordinary rules. Permission to amend may be refused where the amendment tendered fails to state a cause of action.

Johnson v. Anderson, 11 A. B. R. 294, 70 Neb. 233, “* * * the court in the exercise of a reasonable discretion, properly refused to allow the plaintiff to amend his petition, where the amendment tendered failed to allege that the defendant to whom the payment was made by the insolvent within four months before the filing of the petition in bankruptcy, had reasonable ground to believe that by such payment a preference was intended” [now, “would be effected”].

§ 1770¹/₂. **Procedure to Follow Procedure of Forum.**—Whether the suit be instituted in the State or in the federal court, the procedure follows the usual course of procedure of the court where the action is pending.

Westall v. Avery, 22 A. B. R. 673, 171 Fed. 626 (C. C. A. N. Car.): “It is also well settled that a proceeding instituted by a bankrupt’s trustee to set aside fraudulent conveyances or illegal preferences is not a proceedings in bankruptcy but while ancillary to such proceedings and authorized by the Bankruptcy Act to be instituted in either the Federal District Court or in a State Court of competent jurisdiction, it must be governed, so far as pleading and practice are concerned, by the laws and rules of the court where it is instituted.”

§ 1770⁵/₈. **Directing a Verdict.**—Thus, the court, in some jurisdictions may direct a verdict on the question of insolvency.

Utah Ass’n v. Boyle Furniture Co., 31 A. B. R. 488, 39 Utah 518: “One of the principal reasons assigned in the petition for a rehearing why a rehearing should be granted was that we had erred in holding that there was not sufficient evidence of the bankrupt’s insolvency to require a submission of that question to the jury. * * * We have again carefully gone over the whole list of the property claimed by counsel and the valuation put upon it by them, and, without going into the details of setting forth the several items we are more firmly convinced than ever that under no possible view of the evidence could a jury of reasonable men have found that the bankrupt’s property, taken at a fair valuation at the time of the transfer was sufficient to pay his debts which were undisputed. * * * The District Court committed no error in determining as a question of law, that the bankrupt was insolvent at the time of the transfer.”

§ 1770³/₄. **Interest.**—The preferential transferee is chargeable with interest, although it is not clear as to the time from which the interest should begin, whether from the date of the transfer, the date of demand, or the date of notice.

Compare *Ommen, Trustee, v. Talcott*, 23 A. B. R. 572, 175 Fed. 261 (D. C. N. Y. partly reversed but on other grounds, S. C., 26 A. B. R. 689, 188 Fed. 401): “First as regards the question of interest. By December 19th, 1902, the defendant had received clear intimation that the receiver regarded his possession as wrongful, for he attempted by summary order to obtain possession. It is, of course, quite true, at least in theory, that a subsequent trustee might not agree with the receiver, but I am satisfied that the defend-

ant took his chances in retaining possession after that time, and that no demand was necessary. From then he became a trustee *ex maleficio*, having seized from the estate property which he had no right to retain, and which he knew was being claimed. Interest must therefore be charged against him at least from the time when he sold the property, and I can see no reason why he should not pay interest at the legal rate. Were he a duly constituted trustee he would be obliged to pay only such interest as he in fact received or should have got, but I think it will not be contended that he has any such exemption from the time when his retention became wrongful. A question does arise as to interest between December 15th, 1902, and the date of sale of the property, which was all substantially completed by the end of June, 1903. As this suit was in the first instance to obtain the property itself and not an action of conversion, I do not think that interest should be charged against the defendant while the property remained in specie. While the contract authorized the sale, it certainly did not mean to authorize his possession either of the property or of the proceeds. I shall, therefore, charge him with interest at six per cent. from the date of the sale of each article and from the collection of each account."

Utah Ass'n *v.* Boyle Furniture Co., 31 A. B. R. 448, 39 Utah 518: "We are of the opinion that in view of the authorities interest should be allowed from the time it is shown that the transferees wrongfully held the property or money received by him, i. e., from the time a demand is made upon him to return the same, and, in case no formal demand is made, then from the time a suit is instituted to recover back the money or property, since the commencement of an action in itself constitutes a demand. This rule seems to be based upon the theory that before demand for the property or money is made the party receiving and holding the same, although it may constitute a preference, is, notwithstanding, not holding it wrongfully, and that he is not chargeable with interest until he does so."

§ 1770 $\frac{7}{8}$. **Reimbursement for Expenses, etc.**—It has been held that the preferential transferee may not be given compensation nor expenses for the care of the property after notice or demand by the trustee.

Ommen, Trustee, *v.* Talcott, 23 A. B. R. 572, 175 Fed. 261 (D. C. N. Y. partly reversed, but on other grounds, S. C., 26 A. B. R. 689, 188 Fed. 401): "As to the items of 'discharge,' prior to January 15th, they must be all disallowed in accordance with the well-settled rule that any services rendered, or disbursements made, by a trustee *ex maleficio*, are made upon his own account, and cannot be credited to him when he comes to account in a court of equity. There is nothing unjust in this. The defendant wrongfully seized the goods and at once began selling them, which he had no right to do, and which he knew he would be held liable for doing. In selling them he made certain disbursements, but they were not made at the request of the trustee or of receiver or of any other person. By all rules of equity they must be held to be purely voluntary, and he cannot credit himself with them."

SUBDIVISION "D."

RES ADJUDICATA IN ACTIONS BY OR AGAINST TRUSTEES.

§ 1771. **Referee's Order of Allowance or Disallowance, Res Judicata.**—The referee's order of allowance or disallowance of a claim is res

judicata in subsequent actions between the same creditor and the trustee.¹¹

Clendenen v. Red River Valley Nat'l Bk., 11 A. B. R. 245 (Sup. Ct. N. Dak.):
 “* * * referees are judicial officers clothed with power to adjudicate in the first instance over the allowance or disallowance of claims presented against the bankrupt's estate, and their findings are entitled to the respect and credit given to officers acting judicially. * * * It is unnecessary to say that we have no supervisory or appellate jurisdiction over referees in bankruptcy or over the decisions of courts of bankruptcy.

“The question which the plaintiff seeks to have us determine has been judicially determined by a tribunal having jurisdiction, and is therefore binding upon us. *Smith v. Walker*, 77 Ga. 289, 3 S. E. 256. Whether the referee intended to decide these questions is not material. As we have seen, they were necessarily involved, and were in fact determined by his adjudication. Whether, his decision was right or wrong we need not discuss. It is sufficient for the purpose of this case to say that the question has been adjudicated by the order of allowance made by the referee, and that the same has not been reconsidered by him or reversed by the judge upon a petition for review. If the trustee was dissatisfied with the adjudication made by the referee, he had a speedy remedy in the bankruptcy court upon a petition for review, and also by appeal from the order of the bankruptcy court if adverse to him.”

And state courts are without power to review, revise or reverse a referee's order allowing a claim.¹²

In *re Osborne's Sons*, 24 A. B. R. 65, 177 Fed. 184 (C. C. A. N. Y.): “In it depositors in an insolvent national bank in the hands of the comptroller of the currency whose claims had been paid in full were held entitled to interest on the ground that when their claims were proved to the satisfaction of the comptroller they were to be treated as judgments. Mr. Justice Swayne said at page 438: ‘The fiftieth section of the National Banking Act, 13 Stat. 113, requires the comptroller of the currency to apply the moneys paid over to him by the receiver “on all such claims as may have been proved to his satisfaction, or adjudicated in a court of competent jurisdiction.” The act is silent as to interest upon the claims before or after proof or judgment. Can it be doubted that a judgment, if taken, would include interest down to the time of its rendition? Section 996 of the Revised Statutes, page 182, declares that all judgments in the courts of the United States shall bear the same rate of interest as judgments in the courts of the States respectively where they are rendered. Interest is allowed by the law of New York upon judgments from the time they are perfected. Rev. Code of N. Y. (Ed. 1859), Vol. III, page 637. If these claims had been put in judgment, whether in a court of the United States or in a State Court of that State, the result as to interest upon the judgment would have been the same. It was unnecessary to reduce them to judgment, because they were proved to the satisfaction of the comptroller. After they were so proved, they

11. Contra, unless perhaps the same issue were actually litigated, *Buder v. Columbia Distill. Co.*, 9 A. B. R. 331, 70 S. W. 508, 96 Mo. App. 558. Compare, ante, § 1359 and § 791.

Contra, *Credit Men v. Furniture Co.*, 26 A. B. R. 867 (Utah), wherein the court erroneously speaks of an allowance by the “trustee.” The trustee is a party and does not make the order

of “allowance.” It is the referee who, by § 1 of the Bankrupt Act, as “the court of bankruptcy,” makes the order of allowance, and it is *res adjudicata*. There is no such thing as an allowance by the trustee.

12. *Clendenen v. Red River Valley Nat'l Bk.*, 11 A. B. R. 245, 12 N. Dak. 51.

were of the same efficacy as judgments, and occupied the same legal ground. Hence, they are within the equity, if not the letter of these statutes, and bear interest as judgments would have done. Sedgw. on Constr., 311, 315.' We think that allowed claims in bankruptcy are as much entitled to be treated as judgments. Section 57 of the Bankruptcy Act provides that the proof of debts shall be in writing signed and sworn to by the creditor, stating the consideration and other particulars, and when this proof is filed in the court or before the referee the claim shall be allowed unless objected to. The subject is further regulated by General Order XXI and by forms prescribed by the Supreme Court."

So, likewise, are the United States District Courts unless by way of due appeal or on petition for review.

§ 1772. Also His Order Determining Validity and Priority of Liens.—The referee's order determining the validity and priority of a lien on the bankrupt's property is *res judicata*. Thus, a mortgagee of the bankrupt's real estate, to whom, after due hearing, has been awarded the amount of her lien from the proceeds of sale, is protected by the order of the referee, which established her right to the money, until the order is set aside by proceedings directly taken for that purpose.¹³

§ 1773. Referee Not to Impeach Own Order.—A referee will not be permitted to testify that he had not undertaken to pass upon the question of preference when he allowed the claim: it was necessarily involved in the allowance.¹⁴

But he may be permitted to testify that entries in his record book were not authorized by him.¹⁵

§ 1774. Adjudication as to Fraud on Discharge, Not *Res Judicata* in Suit by Trustee.—An adjudication as to the fraudulent character of a transfer, made on the discharge, is not *res adjudicata* in a suit by the trustee to set aside the alleged fraudulent conveyance.

Paxton v. Scott, 10 A. B. R. 80, 92 N. W. 611 (Neb.): "It is now claimed that the discharge operated as a bar to these proceedings, and that the whole question of fraud is *res judicata*, and that the State court had no jurisdiction to proceed further after that decision.

"We are not able to sustain this contention as to the effect of the discharge."

The question has not arisen, however, where the discharge was opposed by the trustee under favor of the Amendment of 1910 to Bankr. Act, § 14 (b). Yet it would seem that that fact would not be sufficient to make it *res judicata*.

§ 1774^{1/4}. Unsuccessful Opposition to Discharge for False Writ-

¹³ In re Wilkesbarre Furn. Mfg. Co., 12 A. B. R. 472, 130 Fed. 796 (D. C. Penn.).

¹⁴ *Clendening v. Red River Valley*

Nat'l Bk., 11 A. B. R. 245, 12 N. Dak. 51.

¹⁵ *Scofield v. U. S. ex rel. Bond*, 23 A. B. R. 259, 174 Fed. 1 (C. C. A. Ohio).

ten Statement Not Res Judicata That Debt Not on False Pretenses.—An unsuccessful opposition to a discharge or composition on the ground of a false statement in writing to obtain credit is not *res judicata* in subsequent litigation that the same debt is not one founded upon false pretences and hence excepted from the operation of discharge.¹⁶

§ 1774½. **Adjudication of Bankruptcy for Fraudulent Transfer Whether Res Adjudicata on Trustee's Suit.**—It has been held, though in an obiter, that an adjudication of bankruptcy on the ground of a fraudulent transfer is not *res adjudicata* in a suit by the trustee to recover the property.¹⁷

§ 1775. **Refusal of Summary Order to Surrender Assets Not Res Adjudicata in Plenary Action.**—The refusal of a summary order is not necessarily *res judicata* in a plenary suit against the same person for the same property; present possession must be proved to obtain the summary order, but is not necessary to a judgment to recover the value of property unlawfully transferred; likewise, the degrees of proof are different.

Murray v. Joseph, 16 A. B. R. 716, 146 Fed. 260 (D. C. N. Y.): "Ordinarily, of course, if a man is sued in a lawsuit, and there is a judgment recovered in that case, he cannot sue again for the same thing. The first judgment determines the question. But this was a summary proceeding, based upon the theory that there was clear and conclusive proof that the parties proceeded against in this case had property in their possession. In those cases, where the proof is perfectly clear and substantially decisive, the courts of bankruptcy exercise a summary jurisdiction in such cases, and order that property be turned over to the trustee; and, if it is not obeyed, the parties under those circumstances are committed to jail for contempt for not obeying the order. But it is perfectly well-settled law that a case may be sufficiently doubtful to prevent the court of bankruptcy from making a summary order in one of those proceedings, although there may be sufficient evidence in the case, such that if it were submitted to a jury on a trial it would justify a verdict against the party, which the court would not feel authorized to set aside. Therefore, it is my opinion that any order made in a proceeding of this kind which does not find the party proceeded against liable to pay over is not a legal bar to a suit brought by a trustee where the evidence can be taken in full, and the jury can pass upon the question."

§ 1776. **Whether Adjudication in Bankruptcy Res Adjudicata as to Insolvency When Act Committed, if Insolvency Essential Element.**—It has been held that the adjudication in bankruptcy will be evidence of the bankrupt's insolvency at and since the act of bankruptcy was committed.¹⁸

16. *Friend v. Talcott*, 228 U. S. 27, 30 A. B. R. 31, quoted at § 2750½ and § 2750¾.

17. Obiter, *In re Larkin*, 21 A. B. R. 711, 168 Fed. 100 (D. C. N. Y.).

Estoppel in One Case by Pleadings Filed in Another Case.—Analogously

Long v. Lackman, 14 A. B. R. 172 (D. C. Colo.).

18. *Breckons v. Snyder*, 15 A. B. R. 112, 116, 211 Penn. St. 176; *In re Virginia Hardwood Mfg. Co.*, 15 A. B. R. 137, 139 Fed. 209 (D. C. Ark.); *Cook v. Robinson*, 28 A. B. R. 182, 194 Fed.

Lazarus v. Egan, 30 A. B. R. 287, 206 Fed. 518 (D. C. Pa.): "While it is true as argued, the filing of a petition and adjudication in bankruptcy does not generally establish the insolvency of the bankrupt at any date prior to such filing, it is equally certain that in the case of an involuntary proceeding where insolvency is one of the issues, the bankrupt, by the adjudication, is conclusively proven to have been insolvent at the time of the commission of the act of bankruptcy. * * *. And it matters not that Egan was actually without notice of these proceedings. An adjudication being an adjudication in rem, all persons interested in the res are regarded as parties to the bankruptcy proceedings. Among such parties are not only the trustee but all creditors, including lienors."

At any rate, if insolvency was a necessary element in the proof of the act.

But the better reasoning seems to be that the doctrine of *res judicata* does not apply in such cases, for the reason that the subject matter in the two cases is not the same. In the first case the status of the debtor is the subject matter, and upon that point the adjudication in bankruptcy is binding upon the whole world, being an adjudication in a proceedings in rem; but in the latter case the subject matter is the property, and though it is also a proceedings in rem, the res is different and the interests of the parties different.¹⁹ It might well be that the debtor should be declared bankrupt and that the creditor might properly desire such result, therefore the creditor should not be bound simply because the desired and proper result were brought about by an allegation and proof involving a transaction in which he was a party. He should only be bound when the ultimate adjudication is one to which he is adverse.

§ 1776 $\frac{1}{4}$. **Adjudication Not Binding on Those Not Entitled to Oppose.**—Of course the adjudication is not binding on those not entitled to oppose. Thus, the adjudication of a partnership is not binding either as to the existence of a partnership or the ownership of alleged partnership assets as against a trustee in bankruptcy of one of the alleged partners.²⁰

§ 1776 $\frac{1}{2}$. **General Adjudication, Where Several Acts Charged, Not Res Adjudicata.**—Where the adjudication is general in its terms and several distinct acts are charged, it is not *res adjudicata* as to any act.²¹

§ 1777. **At Any Rate, Adjudication on Ground of Preference Not Res Judicata on Issue of "Reasonable Cause for Belief."**—At any rate, an adjudication on the ground of preference is not *res judicata* on the issue of the existence of a reasonable cause for belief.²²

753 (C. C. A. Alaska); *Whitwell, trustee, v. Wright*, 23 A. B. R. 747, 136 App. Div. N. Y. 246. But compare, ante, §§ 1362, 445.

19. *Silvey & Co. v. Tift*, 16 A. B. R. 12, 123 Ga. 804. See ante, "Effect of Adjudication in Subsequent Litigation," § 444. Also, ante, § 1362. Also, compare, *Levor v. Seiter*, 5 A. B. R. 576, 69 N. Y. Supp. 987 (reversed, on

other grounds, in 8 A. B. R. 459, 74 N. Y. Supp. 499).

20. *Manson v. Williams*, 22 A. B. R. 22, 213 U. S. 453, quoted ante, § 445.

21. See ante, § 446 $\frac{1}{2}$; also, see *In re Letson*, 19 A. B. R. 506, 157 Fed. 78 (C. C. A. Okla.).

22. *Hussey v. Dry Goods Co.*, 17 A. B. R. 516, 148 Fed. 598 (C. C. A. Kans.), quoted § 446; *Laundy v. Nat'l Bank*, 11 A. B. R. 223, 66 Kan. 759.

§ 1777¹/₈. **No Collateral Attack on Adjudication.**—The adjudication of bankruptcy may not be attacked by an alleged preferential or fraudulent transferee in a suit by the trustee to set aside the transfer, so long as the record of adjudication on its face does not affirmatively show lack of jurisdiction.²³

Huttig Mfg. Co. v. Edwards, 20 A. B. R. 349, 160 Fed. 619 (C. C. A. Iowa): "The manufacturing company attacks the validity of the adjudication that D. Winter was a bankrupt upon the ground that one of the three petitioners in the involuntary proceeding was not a creditor, but since the attack was made in a proceeding by the trustee to annul a preference it is a collateral, not a direct, one. An adjudication of bankruptcy is entitled to the same verity and is no more to be impeached collaterally than other judgments or decrees of courts of competent jurisdiction. It cannot be assailed by the defendant in a suit by the trustee to recover or avoid a preference upon the ground that one of the petitioners was not in fact a creditor of the bankrupt. When the record shows jurisdiction the adjudication of bankruptcy is subject to impeachment only by a direct proceeding in a competent court. *Michaels v. Post*, 21 Wall. 398, 22 L. Ed. 520; *Sloan v. Lewis*, 22 Wall. 150, 22 L. Ed. 832."

§ 1777¹/₄. **Nor on Regularity of Appointment.**—Nor may the regularity of the receivers' or trustees' appointment be attacked in a proceeding by adverse claimants to recover possession of property.²⁴

§ 1777³/₈. **Nor on Administrative Order.**—Nor may the findings of an order surcharging the trustee be collaterally impeached.

Hebert v. Crawford, 228 U. S. 204, 30 A. B. R. 24: "The finding in the summary proceeding that Le Blane received possession as trustee was conclusive against him and was not subject to collateral attack by third persons. *Noble v. Union Pac. Logging Co.*, 147 U. S. 173, 174."

§ 1777¹/₂. **Bankruptcy Court's "Call" or "Assessment" or "Unpaid Stock Subscription."**—The findings of the bankruptcy court, in exercising its jurisdiction to make "calls" or "assessments" upon "unpaid stock subscriptions" to bankrupt corporations are conclusive upon the stockholder in the subsequent plenary suit against him to enforce the same, upon the questions of the necessity and percentage of the "call" or "assessment," and incidentally upon the amounts of the corporate indebtedness and assets respectively, and, probably, if he has been duly notified, also upon the amounts paid in by other stockholders.²⁵

But, it would seem, on principle, that the effect of the "call" or "assessment" by the bankruptcy court would extend no further than to the matters mentioned, and no further than would that of the bankrupt corporation itself, had it made the call or assessment, since the trustee succeeds merely to the bankrupt in performing this function and the

²³. Also, see ante, §§ 30, 437, 441¹/₂, 450.

²⁴. *Ross v. Stroh*, 21 A. B. R. 644, 165 Fed. 628 (C. C. A. Pa.).

²⁵. In re *Remington Automobile Co.*, 18 A. B. R. 389, 153 Fed. 345 (C. C. A. N. Y.), quoted ante, § 977.

stockholder is entitled to have his rights determined in a plenary suit; the proceedings in the bankruptcy court being incapable of as broad an effect as in the ordinary tribunals, which have jurisdiction to render personal judgments against stockholders as well as to make "calls" for unpaid stock subscriptions of insolvent corporation.²⁶

§ 1777³. **Miscellaneous Holdings as to Res Adjudicata.**²⁷—It has been held that failure to oppose the entry of decree of title in the State Registration Court within the statutory time, is no bar to the trustee's suit to set aside the transfer as preferential.²⁸ Where the status of property has already been passed on by the State court, it will be considered res adjudicata in the bankruptcy court.²⁹

It is to be said, in general, that the bankruptcy court is a court of general jurisdiction in bankruptcy matters and that its judgments, decrees and orders possess all the attributes of finality and estoppel accorded to domestic judgments emanating from courts of general original jurisdiction.³⁰

26. Also, see ante, § 977.

27. **Former adjudication as to bankrupt's use of trust funds, when does not conclude infant beneficiary.** In re Tucker, 18 A. B. R. 378, 153 Fed. 91 (D. C. Mass.).

28. *Morris v. Small*, 20 A. B. R. 138, 160 Fed. 142 (D. C. Mass.).

29. In re Seavey, 27 A. B. R. 373,

195 Fed. 825 (D. C. N. Y.).

Re-Examination of Prepaid Attorney's Fee—Order of Bankruptcy Court as Res Judicata in Subsequent Suit against Attorney.—*Henderson v. Denious*, 26 A. B. R. 226, 186 Fed. 100 (C. C. A. Ark.).

30. *Henderson v. Denious*, 26 A. B. R. 226, 186 Fed. 100 (C. C. A. Ark.).

CHAPTER XXXIV.

RECEIVERS AND TRUSTEES AS DEFENDANTS IN PLENARY SUITS.

Synopsis of Chapter.

- § 1778. Receivers and Trustees as Defendants in Plenary Suits.
- § 1779. May Be Made Party Where State Court Has Custody of Res.
- § 1780. May Be Sued in Personam for Conversion or Trespass for Wrongful Seizure.
- § 1780½. Also for Debt Contracted as Receiver.
- § 1781. Such Suits Generally Not Enjoined by Bankruptcy Court.
- § 1782. But May Be Enjoined, if Equity Demands It.
- § 1783. May Be Sued without Leave of Bankruptcy Court.
- § 1784. Need Not Be Sued in Official Capacity, but Merely as Individual.
- § 1785. Execution against Receivers and Trustees.
- § 1786. Orders by Bankruptcy Court to Pay Judgments Out of Funds of Estate.
- § 1786½. Or May Order Indemnity Direct from Estate to Injured Party without Judgment.
- § 1787. Garnishees, etc., as Bankrupts—Trustee to Respond.
- § 1788. Dissatisfied Litigants in Bankruptcy Proceedings Attempting to Obtain Indirect Review by Bringing Independent Suit against Trustee.
- § 1788½. Nor May the Trustee Be Controlled in His Discretion, in the Administration of the Estate by Proceedings Brought in Another Court.

§ 1778. Receivers and Trustees as Defendants in Plenary Suits.

—Receivers and trustees in bankruptcy may be sued elsewhere than in the bankruptcy proceedings.¹

§ 1779. May Be Made Party Where State Court Has Custody of Res.—Where another court has jurisdiction over the res, the parties therein may make the trustee or receiver a party defendant, to cut off his rights.²

Thus, they have been permitted to make him a party defendant to a suit for infringement of a patent.

Victor Talking Machine Co. v. Hawthorne, 23 A. B. R. 234, 173 Fed. 617 (D. C. Pa.): "The complainant now asks leave to file a supplemental bill to make the trustee a party to the suit, and the application is resisted, on the ground that the suit for infringement seeks redress for a tort, with which the bankrupt's estate has no concern, since a claim for damages founded upon a tort, unconnected with a contractual liability, cannot be proved against the assets and is not affected by the discharge. *Re Boston, etc., Iron Works (C. C.)*, 23 Fed. 880; *Re United Button Co. (D. C.)*, 15 Am. B. R. 390, 140 Fed. 495. It is therefore contended that the trustee should not be compelled to appear in such suit and spend the money of the estate in litigation, which may be prolonged and expensive, and can in no way benefit the creditors.

1. In *re Smith*, 9 A. B. R. 603, 121 Fed. 1014 (D. C. N. Y.).

2. In *re Smith*, 9 A. B. R. 603, 121

Fed. 1014 (D. C. N. Y.). Compare ante, §§ 1646, 1650½.

It will be observed, however, that the present motion does not attempt to compel the trustee to make an active defense. It merely asks permission to make him a party, leaving him free to take such action thereafter as he may be advised, or as the bankruptcy court may direct. Certainly he is not bound to defend the suit, if the interest of the estate will not be affected by the litigation; but I can see no good reason for declining to make him a party of record, in order that he may be bound by the decree, so far as that result may properly follow. For example, part of the relief prayed for—the delivery of infringing apparatus to be destroyed—may apply to some of the bankrupt's property that has come into his hands; and in other respects, also, it is impossible to decide upon this motion whether or not the bill may injuriously affect the estate in his charge. In a given case it is readily conceivable that a decree for the complainant might seriously injure a valuable patent belonging to the bankrupt but not directly involved in the suit, and it might therefore be desirable to defend the action. This and like matters are for the trustee's consideration in the first instance, and he may then take whatever steps may seem most advantageous. The order that is now to be entered will only permit the complainant to make him a party. What else, if anything, he should be compelled or permitted to do, is a matter for future consideration by the proper court."

§ 1780. May Be Sued in Personam for Conversion or Trespass for Wrongful Seizure.—Also a receiver or trustee may be sued in the state court in an action in personam for a money judgment for converting property in his possession belonging to another.³

In re Gutman & Wenk, 8 A. B. R. 252, 114 Fed. 1009 (D. C. N. Y.): "The fact that the petitioner was a receiver of a court would not ordinarily afford him immunity for a tortious act."

Or for trespass for wrongful seizure of property belonging to another.⁴

Berman v. Smith, 22 A. B. R. 662, 171 Fed. 735 (D. C. Ga.): "There is no question that suit may be brought in the State courts for wrongful acts of

3. *In re Kanter & Cohen*, 9 A. B. R. 372, 121 Fed. 984 (C. C. A. N. Y.); *In re Mertens & Co.*, 16 A. B. R. 831, 147 Fed. 177 (C. C. A. N. Y.); *In re Foundry & Machine Co.*, 17 A. B. R. 291, 147 Fed. 828 (D. C. Wis.); Conversion for selling mortgaged chattels without notice to mortgagee. *McLean v. Mayo*, 7 A. B. R. 115, 113 Fed. 106 (D. C. N. Car.); *obiter*, *In re Russell & Birkett*, 3 A. B. R. 658, 101 Fed. 248 (C. C. A. N. Y.); compare, *Chauncey v. Dyke Bros.*, 9 A. B. R. 444, 119 Fed. 1 (C. C. A. Ark.); *Welch v. Polley*, 11 A. B. R. 215 (197 N. Y. 177); *In re Spitzer*, 12 A. B. R. 346, 130 Fed. 879 (C. C. A. N. Y.); *impliedly*, *In re Kelly Dry Goods Co.*, 4 A. B. R. 530, 102 Fed. 747 (D. C. Wis.). Instance, *In re Freeman*, 9 A. B. R. 68 (D. C. N. Y.), where such right is assumed to exist. Compare, *impliedly*, *In re Roberts*, 22 A. B. R. 908, 169 Fed. 1022

(C. C. A. N. Y.), quoted at § 1781. See post, § 1814.

Security for Costs on Appeal.—If the trustee be successful his adversary may appeal only on giving the usual bond; and the bankruptcy court will not aid him by staying the trustee. *In re National Lock & Metal Co.*, 19 A. B. R. 106, 155 Fed. 690 (D. C. N. Y.).

4. *In re Spechler Bros.*, 26 A. B. R. 97, 185 Fed. 311 (D. C. N. Y.); *McLean v. Mayo*, 7 A. B. R. 115, 113 Fed. 106 (D. C. N. Car.).

But he may not, at any rate, be sued in equity, *Treat v. Wooden*, 14 A. B. R. 736, 138 Fed. 934 (U. S. C. C. Mass.).

Compare, facts in *In re Grainger*, 20 A. B. R. 166, 160 Fed. 69 (C. C. A. Calif.); compare, *impliedly*, *In re Roberts*, 22 A. B. R. 908, 169 Fed. 1022 (C. C. A. N. Y.), quoted at § 1781.

officers of the bankruptcy court, where they go entirely beyond their duties as such officers and are guilty of conduct which is actionable in its character, particularly as against third persons."

Or for wrongfully detaining property belonging to another.⁵

Skilton v. Codington, 15 A. B. R. 810, 185 N. Y. 80: The court in this case held in substance that where a trustee in bankruptcy retains out of the proceeds of the sale of the bankrupt's property a certain sum for the benefit of any liens or claims that might be established against the property, the State Court has jurisdiction to hear and determine an action brought against such trustee for detaining the property covered by a chattel mortgage executed by the bankrupt and recover the amount due on a note which the mortgage was given to secure, if the bankruptcy court does not enjoin the prosecution of such action.

Thus, he may be sued in personam for damages for wrongfully detaining property from a landlord.

In re Hunter, 18 A. B. R. 477, 151 Fed. 904 (D. C. Pa.): "The landlord having, therefore, been entitled to the possession of his property on April 1st, and the trustee having refused to surrender, the latter became a trespasser and was liable in damages. The direct and immediate consequence of its refusal was that the new tenant threw up the lease, and, as the landlord was not able to find another tenant within the term, he lost the rent for three months. For this sum I think the trustee would be directly and personally liable to be sued."

But compare limitations of rule that such occupancy constitutes trespass, *In re Rubel*, 21 A. B. R. 566, 166 Fed. 131 (D. C. Wis.): "The claimant's attorneys cite the case of *Hunter* (D. C.), 18 A. B. R. 477, 151 Fed. 904, and insist that it is applicable and controlling here. An examination of this case will show that the lease of the bankrupt had expired before the trustee went into possession, and therefore he was held by the court to be a trespasser. In the instant case the receiver and the trustee entered under the lease, and therefore could not be held to be trespassers. The notice to quit provided for by the Wisconsin statute which was served upon the receiver was ineffectual to change the status of the parties. The receiver is not invested with the title, but is a mere custodian, without discretion, and until the trustee was appointed on the 29th day of April there was no legal representative of the estate who was clothed with title or authority in regard to the same. It appears that the trustee occupied the property only two days. The sale was made, and confirmed by the court on the 30th day of April, at which time the trustee abandoned his possession. There was then no reason why the petitioner might not have entered and taken possession on the evening of the 30th day of April. Certainly greater expedition could not have been expected. The fact that the petitioner permitted the purchaser of the stock of goods to remain in the store until the 15th day of May is not to be charged against the trustee."

§ 1780¹/₂. Also for Debt Contracted as Receiver.—There is no rea-

5. Instance, *Orr Co. v. Cushman*, 18 A. B. R. 535 (City Court of N. Y.); *In re Spechler Bros.*, 26 A. B. R. 97, 185 Fed. 311 (D. C. N. Y.): *In re Em-*

pire Construction Co., 166 Fed. 1019 (C. C. A. N. Y., reversing S. C., 19 A. B. R. 704, 157 Fed. 485).

son to suppose that the receiver or trustee may not be sued in plenary actions in personam for debts contracted in carrying on the receivership.⁶

But in such cases it has been held that he may not be sued except in his capacity as receiver, unless he specially binds himself or unless he exceeds his authority.

In *re Kalb & Berger Mfg. Co.*, 21 A. B. R. 393, 165 Fed. 895 (C. C. A. N. Y.): "While, ordinarily, a receiver acting within his powers is not personally liable upon his contracts, yet he may so contract as to bind himself; and if he acts beyond his powers he necessarily assumes individual responsibility. The action in the Municipal Court in so far as it was against the defendant personally could not be stayed by the District Court. The power conferred by the Bankruptcy Act to determine controversies with respect to the collection and distribution of the bankrupt estate, cannot be extended to confer jurisdiction to stay proceedings against officers in their individual capacities. It may be that in this case the receiver acted within the scope of his authority and was not personally liable. If so the Municipal Court will undoubtedly decide in his favor. * * * The order of the District Court staying the action in the Municipal Court in so far as it was brought against the receiver as such, presents a more difficult question, in view of the fact that leave does not appear to have been granted to bring such action."

It has been held that the receiver may be sued in the state court for rent of premises where he had made himself personally liable therefor.^{6a} But where it was agreed that the debt or expense incurred was to be paid out of the bankrupt estate, the receiver will not be held personally responsible therefor.⁷

It has been held that a holder of a receiver's certificate may not sue the receiver in an independent plenary action but must come into the bankruptcy court and apply for an order therein, to pay out of the funds.⁸

Such holders are chargeable with notice of the limitations imposed by the court's order.⁹

Obiter [summary jurisdiction actually exercised; fund ample to pay certificates in full as prior charge on assets], In *re Burkhalter* [*Rogers v. People's Bank*], 24 A. B. R. 553, 179 Fed. 403 (D. C. Ala.): "* * * would the respondent have been entitled to sue the receiver upon his certificate in a plenary suit? The certificate was not an absolute promise to pay. It was a promise to pay only from a fund in court in process of administration and subject only to the orders of the court which was administering it. The payment of the certificate in full was conditioned upon the sufficiency of the fund to answer all claims of equal priority. If insufficient to pay all, proportional payment only could be demanded. The court in whose control the

6. Instance, *Orr Co. v. Cushman*, 18 A. B. R. 535 (City Court of N. Y.). Compare, In *re Empire Cons. Co.*, 166 Fed. 1019, C. C. A. N. Y., reversing S. C., 19 A. B. R. 704, 157 Fed. 495.

6a. *Brooklyn Improvement Co. v. Lewis*, 24 A. B. R. 122, 136 App. Div. N. Y. 861, the facts in this case, however, being somewhat peculiar.

7. *Weller v. Stengel*, 26 A. B. R. 751 (App. Div. N. Y.).

8. Compare ante, § 389, and post, § 1804½.

9. Compare ante, § 385; In *re Burkhalter* (*Rogers v. People's Bank*), 24 A. B. R. 553, 179 Fed. 403 (D. C. Ala.), quoted supra; In *re Erie Lumber Co.*, 17 A. B. R. 687 (D. C. Ga.).

fund was, was alone competent to determine the sufficiency of the fund and the proper proportional payment, if it was insufficient for payment in full. Referring to such certificates, the court, in the case of *Turner v. Peoria & Springfield Railroad Company*, 95 Ill. 134, 35 Am. Rep. 144, said: 'It usually appears on the face of such instruments by what authority they were issued, and for what specific purpose. Holders thereof will always be chargeable with notice of these facts. Considerations of the highest concern to all parties interested in the trust property make it imperative that the court that charges the fund, through its appointed officer, should have the most vigilant care that the property is not improvidently wasted. All persons dealing in such securities must know that payment can only be coerced by application to the court having the control of the trust property for an order upon its acting officer.'

"The respondent, if the money had not been paid to it by the receiver wrongfully and without authority, could have coerced payment only by petitioning the court having control of the fund to direct its receiver to make the payment. It had no right to demand a determination of its right to payment in a plenary suit. Its position is in no way improved by the wrongful payment to it. Hence the respondent cannot complain of the jurisdiction of the bankruptcy court to order it restored upon condition that petitioner shows that there was no existing indebtedness to the respondent when it was paid, and to determine for itself in a summary proceeding the issue as to the existence of such indebtedness, as it would have had exclusive jurisdiction to do if no wrongful payment had been made. This is what the Circuit Court of Appeals determined, since it directed the remanding of the cause with instructions 'that it be referred to the special master to restate the account between the bank and the receiver in conformity with these views;' and not that a plenary suit be instituted by the receiver against the bank to recover the amount so paid."

§ 1781. Such Suits Generally Not Enjoined by Bankruptcy Court.

—And such actions will not be restrained by the bankruptcy courts.¹⁰

In *re Roberts*, 22 A. B. R. 908, 169 Fed. 1022 (C. C. A. N. Y.): "The State suit is brought against the receiver and his clerk personally. The question raised here has already been decided by this court in *In re Kalb & Berger Manfg. Co.*, 21 Am. B. R. 393, 165 Fed. 895. The order of the bankruptcy court, restraining the prosecution of suit in the State Court, is reversed."

In *re Kalb & Berger Mfg. Co.*, 21 A. B. R. 393, 165 Fed. 895 (C. C. A. N. Y.): "The power conferred by the Bankrupt Act to determine controversies with respect to the collection and distribution of the bankrupt estate, cannot be extended to confer jurisdiction to stay proceedings against officers in their individual capacities."

Except where it appears without dispute that the third party cannot possibly have any legal rights to be established by the litigation in the state court.¹¹

¹⁰. In *re Kanter & Cohen*, 9 A. B. R. 372, 121 Fed. 984 (C. C. A. N. Y.); *McLean v. Mayo*, 7 A. B. R. 115, 113 Fed. 106 (D. C. N. Car.); In *re Spitzer*, 12 A. B. R. 346, 130 Fed. 879 (C. C. A. N. Y.); In *re Spechler Bros.*, 26 A. B. R. 97, 185 Fed. 311 (D. C. N. Y.).

Contra, In *re Mertens*, 12 A. B. R.

698, 131 Fed. 507 (D. C. N. Y.), in which case there was a claim, however, that the party suing had twice submitted himself to the jurisdiction of the bankruptcy court.

¹¹. In *re Gutman & Wenk*, 8 A. B. R. 252, 114 Fed. 1009 (D. C. N. Y.).

Yet in one case, injunction was re-

§ 1782. But May Be Enjoined, if Equity Demands It.—Nevertheless, the bankruptcy court has power to prohibit the prosecution thereof if equity so demands.¹²

In *re Gutman & Wenk*, 8 A. B. R. 252, 114 Fed. 1009 (D. C. N. Y.): "But the statutes which permit such actions without leave of court, provide that they should be subject to the general equity jurisdiction of the court in which the receiver was appointed, so far as the same shall be necessary to the ends of justice."

In *re Schermerhorn*, 16 A. B. R. 509, 145 Fed. 341 (C. C. A.): "After various proceedings before the referee the District Court made an order permitting the petitioner to sue the trustee in a State Court, but it was upon an *ex parte* application and showing and without notice to the trustee or his counsel of record. The District Court, upon being advised of the true situation as disclosed by the record, found that its order had been improvidently granted and it promptly vacated it, and enjoined the petitioner from proceeding further in the State Court. There can be no doubt of the power of the court to do this, nor that its power was well exercised."

In *re Mertens*, 12 A. B. R. 706, 131 Fed. 507 (D. C. N. Y.): "Is not the bankruptcy court, in possession of the property, possessed of power and jurisdiction to try and determine this question? Or must it await the trial and determination of a suit for conversion against its officer in the State Court before proceeding to administer the trust and wind up the bankruptcy proceedings? It is conceded that in such a case as this the bankruptcy court may enjoin an action in replevin in the State Court against the receiver or trustee to recover the property. Why may it not enjoin an action in trespass or for conversion brought against the receiver or trustee in bankruptcy in the State Courts to recover the proceeds of a sale of the property or its value as damages for a conversion, based on the claim that the title was in the vendor? Does the one action interfere with the property or the proceedings in the court of bankruptcy any more or less than the other? If so, wherein?"

However, where the lower court had restrained a landlord from prosecuting a suit in personam against the trustee, sounding in tort, on the ground that it was but an indirect method of obtaining rent for use and occupation, claim for which the landlord had delayed presenting as part of the expenses of administration until almost all the funds of the estate had been paid out, the upper court reversed the ruling because the question as to whether the suit really was in tort was one for the state court to determine.¹³

And the bankruptcy court may revoke a leave if improvidently granted.¹⁴

But the receiver or trustee may only be sued in personam, or where the property is not in the custody of the bankruptcy court; and any suit against the receiver or trustee, instituted to recover property in his custody as such, will be restrained.¹⁵

§ 1783. May Be Sued without Leave of Bankruptcy Court.—The

fused even where the bankruptcy court had previously found that the property rightfully belonged in the bankrupt estate. In *re Spechler Bros.*, 26 A. B. R. 97, 185 Fed. 311 (D. C. N. Y.).

¹² Impliedly, *Skilton v. Codington*, 15 A. B. R. 810, 185 N. Y. 80.

¹³ In *re Empire Cons. Co.*, 166 Fed. 1019 (C. C. A. N. Y., reversing 19 A. B. R. 704, 157 Fed. 495).

¹⁴ In *re Schermerhorn*, 16 A. B. R. 509, 145 Fed. 341 (C. C. A.).

¹⁵ See post, § 1798; *Berman v. Smith*, 22 A. B. R. 662, 171 Fed. 735 (D. C. Ga.).

receiver may be sued without leave of the bankruptcy court being first obtained.¹⁶

In *re Kelley Dry Goods Co.*, 4 A. B. R. 528 (102 Fed. 747) (D. C. Wis.): "No leave to sue the receiver in such case is necessary under the recent legislation of Congress."

But under the Federal statutes¹⁷ he may be sued "as receiver" without leave only "in respect to some act or transaction of his in carrying on the business;" and if he be not carrying on the business or if the matter be not one occurring in the carrying on of the business, he may not be sued except on leave.

In *re Kalb & Berger Mfg. Co.*, 21 A. B. R. 393, 165 Fed. 895 (C. C. A. N. Y.): "Suits against receivers, as a general rule, cannot be brought in any other court than that of their appointment, without leave previously obtained from such court. An exception to this rule exists under certain conditions in case of Federal receivers. The statute (Act March 3, 1887, and August 13, 1888) provides in substance that a receiver appointed in a Federal court may be sued without leave of the court 'in respect to any act or transaction of his in carrying on the business connected with' the property in his charge. It is held that this statute applies to receivers appointed in bankruptcy proceedings as well as other Federal receivers. In *re Kanter and Cohen*, 9 Am. B. R. 372, 121 Fed. 984; In *re Smith*, 9 Am. B. R. 603, 121 Fed. 1014; In *re Kelley Dry Goods Co.*, 4 Am. B. R. 528, 102 Fed. 747. But such receivers cannot be sued without leave unless they are carrying on the business of the bankrupt estate, as they may be authorized to do by the bankruptcy court. In the present case, however, it does not appear that the receiver was authorized to carry on or was carrying on the business. In this transaction he merely arranged for the storage of certain machinery which had come into his possession as receiver. His act related to the care and preservation of the property but had no relation to any business carried on by him. In our opinion the contract of the receiver for the use of the premises was not an act or transaction in carrying on the business, within the meaning of the statute. The action against the receiver as such having been brought without leave of the court which appointed him—the District Court—was properly enjoined by that court. This having been done the District Court went forward and determined the terms of the contract between the parties and the amount due thereunder."

§ 1784. Need Not Be Sued in Official Capacity, but Merely as Individual.—The receiver or trustee, it appears, need not be sued in his official capacity, but merely as an individual,¹⁸ at least in cases where he has personally obligated himself or exceeded his authority.¹⁹

¹⁶. Stats. at Large, 25 U. S. 436; In *re Smith*, 9 A. B. R. 603, 121 Fed. 1014 (D. C. N. Y.); In *re Kanter & Cohen*, 9 A. B. R. 372, 121 Fed. 984 (C. C. A. N. Y.).

No Suit against Receiver upon Claim against Estate of Bankrupt.—Claims against the bankrupt must be presented for allowance against the estate. Suits against the receiver thereon will not be permitted. In

re Heim Milk Product Co., 25 A. B. R. 746, 183 Fed. 787 (D. C. N. Y.).

¹⁷. Stats. at Large, 25 U. S. 436.

¹⁸. In *re Gutman & Wenk*, 8 A. B. R. 252, 114 Fed. 1009 (D. C. N. Y.); inferentially, *McLean v. Mayo*, 7 A. B. R. 115, 113 Fed. 106 (D. C. N. Car.); inferentially, In *re Spechler Bros.*, 26 A. B. R. 97, 185 Fed. 311 (D. C. N. Y.).

¹⁹. Compare ante, §§ 1780, 1780½, 1783.

§ 1785. **Execution against Receivers and Trustees.**—Levy of execution upon a judgment obtained in such suit against the receiver or trustee doubtless may be made out of the receiver's or trustee's individual estate, the bankruptcy court determining whether reimbursement be proper out of the estate.

Compare, *obiter*, *Treat v. Woodin*, 14 A. B. R. 737, 138 Fed. 934 (C. C. Mass.): "How far the Court of Appeals would permit the action of *trover* to proceed, and upon what property it would permit a levy of execution, does not appear. To levy execution upon the individual estate of a trustee in bankruptcy in order to satisfy a judgment for damages arising from his compliance with an order for the sale of specific property made by a court of competent jurisdiction seems to bear hardly upon the trustee. Even the Court of Appeals, however, expressly refused to disturb the control of the court of bankruptcy over the bankrupt estate."

§ 1786. **Orders by Bankruptcy Court to Pay Judgments Out of Funds of Estate.**—The bankruptcy court may, by order, require the receiver or trustee to comply with the judgment or decree against him out of the funds of the estate, if there are any funds. But the bankruptcy court may not so order where there are no funds.

In *re Howard*, 12 A. B. R. 462, 130 Fed. 1004 (D. C. Calif.): "The judgment of the Circuit Court, in so far as it relates to costs, can only be enforced by execution or action. It cannot be enforced in this summary proceeding, as it is conceded that there are not now, and never have been any funds in the hands of the trustee belonging to the petitioner or to the estate of the bankrupt with which to satisfy the same. The motion that the trustee be directed to pay such costs is denied, without prejudice to the right of the petitioner to enforce judgment for the same by action or execution as he may be advised."

§ 1786½. **Or May Order Indemnity Direct from Estate to Injured Party without Judgment.**—Or the bankruptcy court may, where all the parties are before it, order such indemnity paid direct to the injured party without the necessity of a judgment against the trustee.

In *re Hunter*, 18 A. B. R. 477, 151 Fed. 904 (D. C. Pa.): "Ordinarily, no doubt, a claim for damages against a trustee should first be prosecuted to judgment, in order that he may have an opportunity to make defense against the charge of wrongdoing; but, as the present trustee is a party to this proceeding with a full opportunity to be heard, and has made no sufficient defense, and as all parties in interest are before the court, I feel justified in treating the case as if recovery had already been had against the trustee. "If, therefore, the bankrupt estate ought to indemnify the trustee, I see no reason why the indemnity should not be paid directly to the landlord."

§ 1787. **Garnishees, etc., as Bankrupts—Trustee to Respond.**—Where a garnishee goes into bankruptcy his trustee may be required to re

spond.²⁰ But no judgment can be rendered on the garnishment that can be enforced against the trustee except in the bankruptcy court itself. And the garnishment proceedings will be stayed until the dividend sought to be subjected can be ascertained.²¹

§ 1788. Dissatisfied Litigants in Bankruptcy Proceedings Attempting to Obtain Indirect Review by Bringing Independent Suit against Trustee.—Dissatisfied litigants cannot obtain an indirect review of orders made in the proceedings in bankruptcy by instituting plenary actions against the trustee.

Thus, the United States District Court will not entertain an action to restrain the trustee from complying with an order to pay dividends.²²

§ 1788½. Nor May the Trustee Be Controlled in His Discretion, in the Administration of the Estate by Proceedings Brought in Another Court.—Nor may the trustee be controlled in his discretion in the administration of the estate, by proceedings brought in another court. Thus, the bankrupt will not be permitted to enjoin the trustee by a suit in equity in the State court, from carrying out a compromise of a controversy with the bankrupt's wife.²³

^{20.} In re St. Albans Fdy. Co., 4 A. B. R. 594 (D. C. Vt.).

^{21.} In re St. Albans Fdy. Co., 4 A. B. R. 594 (D. C. Vt.).

^{22.} Hatch v. Curtin, 16 A. B. R. 629, 146 Fed. 200 (C. C. Mass.). Ante, §§ 1693, 1700.

^{23.} In re Kranich, 23 A. B. R. 550, 174 Fed. 908 (D. C. Pa.); obiter, In re Spechler Bros., 26 A. B. R. 97, 185 Fed. 311 (D. C. N. Y.). Also, see §§ 1910½, 898¼.

CHAPTER XXXV.

LIMITATIONS OF PLENARY ACTIONS BY AND AGAINST TRUSTEES.

Synopsis of Chapter.

§ 1789. Limitation of Plenary Actions by and against Trustees.

§ 1790. No Suit to Recover Property after Two Years from Closing of Estate.

§ 1791. Not Barred by Expiration of State Limitation after Bankruptcy and before End of Two Years.

§ 1792. Otherwise, State Limitations Prevail.

§ 1793. Nondiscovery of Fraud as Tolling Bar.

§ 1789. Limitation of Plenary Actions by and against Trustees.—The trustee may not bring action nor be sued subsequently to two years after the closing of the estate, but within that period state statutes of limitation are suspended, except as to causes of action barred thereby before the bankruptcy.

§ 1790. No Suit to Recover Property after Two Years from Closing of Estate.—The trustee may not institute legal proceedings subsequently to two years after the estate is closed.¹

§ 1791. Not Barred by Expiration of State Limitation after Bankruptcy and Before End of Two Years.—Suit may be commenced by the trustee upon any action that was not barred by limitation at the beginning of the bankruptcy, and may be so commenced at any time within the two years after the closing of the estate, notwithstanding the State statute of limitations may bar the action before the two years have expired.² In short, the Act creates a new statute of limitations, except as to actions already barred when the bankruptcy proceedings were instituted. It has been held that the statutes of limitation of the states do not apply to actions by trustees under § 60b of the Bankruptcy Act.

Arnold Grocery Co. v. Shackelford (Ga.), 31 A. B. R. 119: "The statute of limitations for the institution of actions on open accounts or for breach of con-

1. Bankr. Act, § 11 (d): "Suits shall not be brought by or against a trustee of a bankrupt estate subsequent to two years after the estate has been closed."

Kinder v. Scharff, 26 A. B. R. 765 (Sup. Ct. La.); *Grunsfeld v. Brownell*, 11 A. B. R. 601 (New Mex. Sup. Ct.); *obiter*, *Sheldon v. Parker*, 11 A. B. R. 152, 66 Neb. 610. But compare, *Evans v. Staale*, 11 A. B. R. 182, 92 N. W. 951 (Minn.).

2. *Sheldon v. Parker*, 11 A. B. R. 152, 66 Neb. 610.

Query, if Estate Reopened after the Two Years, Is Bar of Statute of Limitations Tolled?—An estate once closed

may be reopened after two years because it is not a "suit" within the meaning of the statute. *In re Paine*, 11 A. B. R. 351, 127 Fed. 246 (D. C. Ky.).

The question then arises whether, on the estate being again closed, the statute of limitations is again tolled for a further period of two years. There appears to be no case decided on the point.

The trustee's bond remains liable for two years after the closing of the estate. *Obiter*, *In re Kajita*, 13 A. B. R. 19 (D. C. Hawaii).

tract expressed or implied, as set forth in the Georgia Civil Code 1910, §§ 4362-68, does not apply to an action by a trustee in bankruptcy, under § 60b of the Bankruptcy Act, for goods received by the bankrupt in payment of a pre-existing debt less than four months prior to the filing of the petition in bankruptcy.

"The Bankruptcy Act which conferred upon trustees in bankruptcy the right to institute actions of the character mentioned in the preceding note, also by § 11d, fixed a statute of limitations applicable to such conditions. The action was not barred.

"Under the Bankruptcy Act of 1867 the actions by or against an assignee in bankruptcy, touching any property transferred to or invested in such assignee, were required to be brought within two years from the time when the cause of action accrued for or against the assignee. This was applied as a statute of limitations. *Freelander v. Holoman*, 9 N. B. R. 331, Fed. Cas. No. 5081; *Avery v. Cleary*, 132 U. S. 604; *Jenkins v. International Bank*, 106 U. S. 571; *Bailey v. Glover*, 88 U. S. 342 [1867]: 'Congress has said to the assignee: You shall commence no suit two years after the cause of action has accrued to you, nor shall you be harassed by suits when the cause of action has accrued more than two years against you. Within that time the estate ought to be nearly settled up and your functions discharged, and we close the door to all litigation not commenced before it has elapsed.'

§ 1792. **Otherwise, State Limitations Prevail.**—Otherwise than as above described, the state statutes of limitation will prevail.³

§ 1793. **Nondiscovery of Fraud as Tolling Bar.**—Where the bar of the statute of limitations is tolled by the nondiscovery of the fraud, the pleader need not set forth the particulars of, nor reasons for, the nondiscovery.⁴

3. Instance, *Lehman v. Crosby*, 3 A. B. R. 662 (D. C. N. Y.); *Beattys v. Straiton*, 25 A. B. R. 808, 142 App. Div. N. Y. 369.

4. *Lehman v. Crosby*, 3 A. B. R. 662 (D. C. N. Y.). Instance where statute not tolled. *Beattys v. Straiton*, 26 A. B. R. 808, 142 App. Div. N. Y. 369.

CHAPTER XXXVI.

SUMMARY JURISDICTION OVER THE BANKRUPT, HIS AGENTS AND PERSONS NOT ADVERSE CLAIMANTS; ALSO OVER PROPERTY IN CUSTODY.

Synopsis of Chapter.

§ 1796. Possession of Res, Test of Summary Jurisdiction.

DIVISION 1.

§ 1797. Jurisdiction Once Attaching, Complete for All Purposes.

§ 1798. All Actions to Be Taken in Bankruptcy Court.

§ 1798½. Thus Replevin Suits Not Maintainable.

§ 1799. Thus, Landlord's Forcible Detainer Suits Not Maintainable nor Dis-
traint.

§ 1800. Property Taken Out of Custody, etc., after Bankruptcy, Summarily
Ordered Returned.

§ 1801. Even Property Voluntarily Surrendered by Bankruptcy Receiver or
Trustee, Still within Summary Jurisdiction.

§ 1802. Similarly, Payments or Other Transfers by Bankrupt after Filing of
Bankruptcy Petition.

§ 1803. Whether Recovery Be Plenary or Summary.

§ 1804. Purchasers at Sales by Trustees or Receivers Subject to Summary Ju-
risdiction.

§ 1804½. Holders of Receivers' Certificate.

§ 1805. Obstructive Suits Brought after Bankruptcy Court Acquires Custody.

§ 1806. Thus, Foreclosure Suits, Where Bankruptcy Court Already Has Custody.

§ 1806¼. Attempts to Control Bankruptcy Administration by Injunctions, etc.,
in Other States.

§ 1806½. Interference Otherwise than by Suit.

§ 1807. What Constitutes "Custodia Legis" and "Assumption of Jurisdiction."

§ 1808. As to Adjudication in Bankruptcy "Ipso Facto" Passing Bankrupt's
Property into Custodia Legis.

§ 1809. Real Estate Generally Considered in Bankrupt's Possession.

§ 1810. Mere Rights of Action in Personam, Not Property "in Possession" of
Bankrupt.

§ 1811. Whether Action to Be in Bankruptcy Proceedings Themselves, or Sep-
arate Plenary Action Maintainable in United States District Court.

§ 1812. Nor in State Court, nor in United States District Court.

§ 1813. Bankruptcy Court Permitting Controversies over Property in Its Pos-
session to Be Carried on Elsewhere.

§ 1814. Suits in Personam against Trustees and Receivers.

§ 1814½. Adverse Claimants Not to Be Defeated by Bankruptcy Court Sur-
rendering Custody.

DIVISION 2.

§ 1815. Where Summary Orders Will Lie on Bankrupts, and Persons Not
Adverse Claimants—In General.

§ 1815½. Existence Also of Plenary Jurisdiction Does Not Preclude.

§ 1816. Outstanding Claims by Third Parties on Property in Hands of Bank-
rupt or Agent, Summary Jurisdiction Not Divested.

- § 1817. But Beneficial Interest in Trustee Must Exist.
- § 1818. Order of Surrender before Appointment of Trustee and Even before Adjudication.
- § 1819. Summary Orders on Bankrupt.
- § 1820. No Matter in What Capacity Bankrupt Holds.
- § 1821. Officers of Bankrupt Corporation, Subject.
- § 1822. Summary Orders on Agents and Others.
- § 1822½. State Institution as Depositary of Funds of Bankrupt Estate.
- § 1823. Corporation Agent of Bankrupt, Subject Thereto.
- § 1823½. Bankrupt's Attorney, When Subject Thereto.
- § 1824. Part Adversely Held, Part Held as Agent or Not under Claim of Beneficial Interest.
- § 1825. Lienholder in Possession after Satisfaction of Lien.
- § 1826. Whether Filing of Petition to Redeem from Undisputed Liens Gives Summary Jurisdiction to Order Surrender on Tender of Amount Due.
- § 1827. Custodians and Court Officers in Possession under Nullified Legal Proceedings, Not "Adverse Claimants."
- § 1828. But, until Liens Nullified, Custodians and Court Officers "Adverse Claimants."
- § 1829. Court Officers Holding under Nullified Legal Proceedings Subject to Summary Order.
- § 1830. Order May Not Require Surrender of More than Is in Officer's Hands.

Subdivision "A."

- § 1831. Procedure on Summary Petitions, in General.
- § 1832. What Is Summary Process.
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- § 1834. Right of Trial by Jury Not Violated Thereby.
- § 1835. Bankrupt Ordered to Execute Necessary Papers.
- § 1836. Referee Has Jurisdiction to Make Summary Order.
- § 1837. Written Petition Requisite.
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- § 1838½. Order to Show Cause.
- § 1839. Due Hearing Requisite.
- § 1840. Courts Proceed with Great Caution in Granting Summary Orders.
- § 1841. Punishment for Disobedience of Summary Order, Not Imprisonment for Debt.
- § 1842. Clear, Certain, Convincing or Satisfactory Proof, or Proof beyond Reasonable Doubt, Requisite.
- § 1843. Bankrupt's Sworn Denial Not Conclusive.
- § 1844. But Almost Incontestable Evidence Requisite to Overcome It.
- § 1845. Proof of Present Possession or Control Requisite.
- § 1846. Similarly, Agents and Court Officers Not Subject to Summary Orders as to Disbursements Already Made.
- § 1847. Likewise, No Interest to Be Included.
- § 1848. Whether Possession at Time of Filing Summary Petition or of Granting Order, Requisite.
- § 1849. Circumstantial Evidence Sufficient.
- § 1850. Presumption of Continued Possession When Property Once Traced and Shortage Unexplained.
- § 1851. Rejecting Improbable Explanations.
- § 1852. No Presumption of Continued Possession if Circumstances Raise Counter Presumption.

- § 1853. Order to Describe Property—Orders to Pay Value of Goods, Alternative Orders, etc.
- § 1854. Review of Summary Orders—Set Aside Only for Manifest Error.
- § 1855. Whether "Review" or "Appeal."
- § 1856. Contempt for Disobedience of Summary Orders.
- § 1857. Whether Evidence on Which Order for Surrender Based May Be Re-Examined.
- § 1858. Opportunity Must Be Given to Defend on Contempt.
- § 1859. Evidence on Contempt to Be beyond Reasonable Doubt.
- § 1859½. Whether "Petition for Revision" or "Writ of Error" to Review Contempt Proceedings.
- § 1860. Procedure on Obtaining Surrender from Court Officers.
- § 1861. If Application Be to State Court Whose Officer in Control, Procedure Follows That of Such Court.
- § 1862. If Application Be to Bankruptcy Court, Procedure Follows Ordinary Rules as to Summary Orders on Bankrupts and Agents.
- § 1863. Jurisdiction to Determine Facts Requisite to Summary Jurisdiction.
- § 1864. But Will Only Examine Far Enough to Ascertain if Facts Alleged in Good Faith and if True Would Constitute "Adverse" Party.
- § 1865. Whether Concluded by Pleadings.
- § 1866. Notice Served Outside District Not Sufficient to Confer Jurisdiction to Make Inquiry.
- § 1867. Ancillary Jurisdiction in Bankruptcy Court of Another District to Make Summary Order.

DIVISION 3.

- § 1868. Jurisdiction to Redeem Property from Liens.
- § 1869. Procedure—Petition to Redeem and Notice.
- § 1870. Gives Jurisdiction to Order Cancellation, Assignment or Release, on Tender of Amount Due.
- § 1871. May Not, under Guise of Petition to Redeem, Gain Jurisdiction over Adverse Claimants in Possession.

DIVISION 4.

- § 1872. Summary Jurisdiction to Order Trustee to Surrender Property to Rightful Owner.
- § 1873. Thus, to Order Surrender of Property Belonging to Third Parties.
- § 1874. Referee Has Jurisdiction.
- § 1875. Replevin Suits Not Maintainable against Trustee or Receiver.
- § 1876. Petitions for Reclamation, Surrender or Redelivery.
- § 1877. Reclamation of Property Left for Repairs, Storage or Other Bailment.
- § 1877¼. Of Property Sold on Approval, etc.
- § 1877½. Of Consigned Property.
- § 1878. Of Property Bought on Conditional Sale.
- § 1879. Of Goods Bought under Misrepresentations or While Grossly Insolvent.
- § 1879¼. Election to Rescind.
- § 1879½. Delay in Rescission.
- § 1879¾. Subrogation to Right of Reclamation.
- § 1880. Reclaiming Part Still in Trustee's Hands, Proving Claim for Balance.
- § 1881. Goods Stopped in Transitu.
- § 1882. Converted Property or Its Traced Proceeds, Reclaimable.
- § 1883. "Tracing Trust Funds."
- § 1884. Commingling of Trust Funds or Trust Property.

- § 1884¾. Evidence.
- § 1884½. Goods in Warehouse or Elevator, and Outstanding Receipts.
- § 1884¾. Costs and Expenses on Reclamation or on Surrender of Trust Funds.

DIVISION 5.

- § 1885. Jurisdiction to Marshal Liens.
- § 1886. Consent of Lienholder Not Necessary.
- § 1887. Incidental Power to Compel Execution of Papers by Third Parties.
- § 1887¾. Incidental Power to Reform Instruments.
- § 1887½. And to Relieve against Forfeiture.
- § 1888. Referee Has Jurisdiction.
- § 1889. Reasonable Notice to Lienors or Other Parties in Interest Requisite.
- § 1890. "Ten Days Notice by Mail" Insufficient; "Order to Show Cause," Proper Method.
- § 1891. Notice on Nonresidents, if Court Has Actual Possession.
- § 1892. But Mere Possession of Res and Service of Notice Insufficient to Render Judgment in Personam.
- § 1893. Third Parties May Intervene.
- § 1894. Pleadings and Practice in Marshaling Liens and Interests.
- § 1894½. Statutory Regulations of Right to Institute or Maintain Suit Not Applicable.
- § 1895. Whether Proceedings to Marshal Liens on Property in Custody, on Notice, Strictly "Summary" Proceedings.
- § 1896. What Law Governs Validity.
- § 1897. Where Rights under State Statute Dependent on Resort to Special Remedies.
- § 1898. Rights of Priority under State Statutes as Related to Marshaling of Liens on Property.
- § 1899. "Surrender of Preference" on Distinct Transaction Not to Be Required as Prerequisite to Validity of Lien Which Itself Is Not a Preference.

DIVISION 6.

- § 1900. Summary Jurisdiction to Prevent Trustee Interfering with Others' Rightful Custody.

DIVISION 7.

- § 1901. Jurisdiction to Issue Injunctions in Aid of Bankruptcy Proceedings.
- § 1902. Restraining Sale or Distribution under Levy Made within Four Months.
- § 1903. But no Injunction Where Levy Not Made within Four Months.
- § 1904. And Injunction May Be Refused on Ground of Comity.
- § 1904½. And Where State Officers to Be Restrained, Court Cautious.
- § 1905. Adverse Claimants Restrained until Appropriate Action Can Be Taken.
- § 1906. Adverse Claimants Restrained from Interfering with Assets in Custody of Bankruptcy Court.
- § 1907. Court Proceedings Restrained until Trustee Elected and Appropriate Action Taken.
- § 1908. Court Proceedings Enjoined Where Property in Custody of Bankruptcy Court Sought to Be Seized or Levied on.
- § 1909. Injunction Refused Where Legal Proceedings Not Nullified by Bankruptcy, and State Court Prior in Custody.
- § 1909½. Foreclosure Enjoined Where Actual Possession Afterwards Acquired by Bankruptcy Court.
- § 1910. Whether May Restrain Levy on Exempt Property for Other Purposes than to Interpose Discharge.

- § 1910½. Attempts to Control Trustee's Administration by Proceedings in Other Courts.
- § 1911. Suits in Personam against Receiver, Trustee or Marshal for Wrongful Seizure Not Restrained.
- § 1911½. Staying Trustee's Administration of Estate.
- § 1912. Ancillary Injunction in Aid of Bankruptcy Proceedings in Another District.
- § 1913. No Enjoining of Pledgee's Sale, unless Fraud or Oppression Exist.
- § 1914. Injunction Where Legal Action Requisite to Fix Liability of Sureties.
- § 1915. No Restraining Order to Prevent Proceeding with Levy on Exempt Property after Same Set Apart.
- § 1916. Bankruptcy Petition "Caveat to All the World" and "Attachment and Injunction."
- § 1917. No Injunction before Filing of Bankruptcy Petition to Preserve Status Quo.
- § 1917½. Injunction after Sale by Trustee.
- § 1918. Referee Has Jurisdiction to Issue Restraining Order, Except upon Courts or Court Officers.
- § 1919. Petition Requisite and to Be Filed in Bankruptcy Proceedings Themselves.
- § 1920. Petition to Be Verified.
- § 1921. Notice to Be Given, unless for Good Cause Dispensed with.

DIVISION 8.

- § 1922. Jurisdiction to Punish for Contempts for Interference with Custody.
- § 1923. Restraining Order Not Prerequisite.

§ 1796. Possession of Res, Test of Summary Jurisdiction.—The determination of the questions, first, as to whether the property is tangible or merely a debt, and second, if existing in tangible form, as to who has possession or control of it, determines the forum to which the parties must resort to work out their rights and the manner of procedure, as to whether summary or plenary.

If the possession, actual or constructive, of the property is in the bankrupt, or in his agent, or in someone not claiming a beneficial interest in it, or is in the receiver, marshal or trustee in bankruptcy, the bankruptcy court has summary jurisdiction over it by orders made in the bankruptcy proceedings themselves, and may summarily order its surrender or delivery;¹ may bring all parties claiming interests in it into court; may determine all rights to it; if, on the other hand, some third party claiming some beneficial interest in the property has possession (except in certain instances where court officers are in possession), or if the property does not exist in tangible form, but is a mere debt owed by the third party, then such third party need not come into the bankruptcy pro-

1. In re Logan, 28 A. B. R. 543, 196 Fed. 678 (D. C. N. Y.).

ceedings for his rights, and the trustee cannot bring him into the proceedings, and he is entitled to be heard in plenary action.²

2. In re Teschmacher & Mrazay, 11 A. B. R. 549, 550, 127 Fed. 728 (D. C. Penn.); quoted ante, § 1652; In re Briskman, 13 A. B. R. 57, 132 Fed. 201 (D. C. N. Y.); In re Schermerhorn, 16 A. B. R. 509, 145 Fed. 341 (C. C. A.), quoted post, § 1795 and § 1807. Inferentially, In re Rochford, 10 A. B. R. 608, 124 Fed. 182 (C. C. A. S. Dak.); Pub. Co. v. Hutchinson Co., 17 A. B. R. 427 (Sup. Ct. Mich.); In re Buntrock Clothing Co., 1 A. B. R. 454, 92 Fed. 886 (D. C. Iowa); In re New England Piano Co., 9 A. B. R. 772, 122 Fed. 937 (C. C. A. Mass.); In re McBride & Co., 12 A. B. R. 83, 132 Fed. 285 (Ref. N. Y.); inferentially, In re Cohn, 3 A. B. R. 421 (D. C. N. Y.).

But see an apparent disregard of this principle in In re Pratesi, 11 A. B. R. 319, 126 Fed. 588 (D. C. Del.), where a liveryman in possession at the time of bankruptcy under his lien was held subject to the summary jurisdiction of the bankruptcy court.

Also see, for an apparent confusion of ideas on this point, In re Young, 7 A. B. R. 14, 111 Fed. 158 (C. C. A. Ark.), a case rightly decided (for the bankrupt clearly had the actual custody at the time of bankruptcy) but wrongly reasoned. In re Wells, 8 A. B. R. 76, 114 Fed. 222 (D. C. Mo.).

In re Moody, 12 A. B. R. 724, 131 Fed. 525 (D. C. Iowa), quoted at § 1797; obiter, In re Rudnick, 20 A. B. R. 33, 160 Fed. 903 (C. C. A. N. Y.); impliedly, Knapp & Spencer Co. v. Drew, 20 A. B. R. 355, 160 Fed. 413 (C. C. A. Neb.); impliedly, In re Walsh Bros., 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa), quoted at § 1488; In re Landis, 18 A. B. R. 483, 151 Fed. 496 (D. C. Pa.), quoted at § 1800; In re Coffey, 19 A. B. R. 148 (Ref. N. Y.); Goodnough Mercantile & Stock Co. v. Galloway, 19 A. B. R. 244, 156 Fed. 504 (D. C. Ore.); partially, Clemishaw v. Int. Shirt and Collar Co., 21 A. B. R. 616, 165 Fed. 797 (D. C. N. Y.); impliedly (attempted settlement before bankruptcy, undistributed portions of settlement money still in hands of lender's agent, no jurisdiction in bankruptcy court), In re Smyth, 21 A. B. R. 853, 167 Fed. 871 (D. C. Pa.); Bray v. U. S. Fidelity & Guaranty Co., 22 A. B. R. 363, 170 Fed. 639 (C. C. A. W. Va.), quoted at § 1813; impliedly,

In re Bluestone Bros., 23 A. B. R. 264, 174 Fed. 53 (D. C. W. Va.), quoted at § 1908; In re MacDougall, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.); In re New England Breeders' Club, 23 A. B. R. 689, 175 Fed. 501 (D. C. N. H.); In re Elletson Co., 23 A. B. R. 530, 174 Fed. 859 (D. C. W. Va.), quoted at § 1888; obiter, In re Peacock, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.); In re Donnelly, 26 A. B. R. 304, 188 Fed. 1001 (D. C. Ohio); In re Loveland, 29 A. B. R. 560, 200 Fed. 136 (C. C. A. Mass.); Le Master v. Spencer, 29 A. B. R. 264, 203 Fed. 210 (C. C. A. Colo.); In re Bacon, 28 A. B. R. 565, 196 Fed. 986 (D. C. N. Y.); In re Schoenfield, 27 A. B. R. 64, 190 Fed. 53 (D. C. W. Va., affirmed Salsburg v. Blackford, 29 A. B. R. 320, 204 Fed. 438, C. C. A. W. Va.); instance, In re Clifford D. Mills, 25 A. B. R. 278, 179 Fed. 409 (D. C. N. Y.); Johnston v. Spencer, 27 A. B. R. 800, 195 Fed. 215 (C. C. A. Colo.); obiter [summary jurisdiction denied where bank held deposit], In re Zotti, 26 A. B. R. 234, 186 Fed. 84 (C. C. A. N. Y., affirming S. C., 23 A. B. R. 304, 178 Fed. 304), quoted at § 1807; Clay v. Waters, 24 A. B. R. 293; 178 Fed. 385 (C. C. A. Mo.), quoted at §§ 1800, 1807, 1811, 2331½, 2343¼, 2864; impliedly, In re Hays, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio), quoted at § 1665; impliedly, In re Tarbox, 26 A. B. R. 432, 185 Fed. 985 (D. C. Mass.), quoted at § 1864; impliedly, In re Zehner, 27 A. B. R. 536, 193 Fed. 787 (D. C. La.).

Also see, for apparent confusion arising through failure to ascertain who was in actual possession or control of real estate, the report of the case being absolutely silent on this important point, In re Pickens & Bro., 26 A. B. R. 6, 184 Fed. 954 (D. C. Ga.).

As to jurisdiction to re-examine prepayments to attorneys in bankruptcy, see post, § 2099.

As to jurisdiction to vacate or modify orders "after term," see §§ 439, 858.

No "terms of court" in bankruptcy, see §§ 439, 858, notes.

Summary jurisdiction not precluded, in proper cases, by existence also of plenary jurisdiction. In re Holbrook Shoe & Leather Co., 21 A. B. R. 511, 165 Fed. 973 (D. C. Mont.).

Murphy *v.* Hoffman, 211 U. S. 562, 21 A. B. R. 487: "Before going further it is well to ascertain the principles of law which are applicable to the situation. The Bankrupt Act * * * as originally enacted, did not confer jurisdiction on the District Courts of the United States over suits brought by trustees in bankruptcy to assert title to property as assets of the bankrupt, or to set aside transfers made by the bankrupt in fraud of the creditors or by way of preference, unless by consent of the defendant. *Bardes v. First Nat. Bank*, 178 U. S. 524, 4 Am. B. R. 163, * * *; *Frank v. Vollkommer*, 205 U. S. 521, 17 Am. B. R. 806. * * * The act, however, preserves the jurisdiction, otherwise existing by statute, of the courts of the United States, though it is limited to courts where the bankrupt himself could have prosecuted the action. *Bush v. Elliott*, 202 U. S. 477, 15 Am. B. R. 656. * * * But, where the property in dispute is in the actual possession of the court of bankruptcy, there comes into play another principle, not peculiar to courts of bankruptcy, but applicable to all courts, Federal or State. Where a court of competent jurisdiction has taken property into its possession, through its officers, the property is thereby withdrawn from the jurisdiction of all other courts. The court, having possession of the property, has an ancillary jurisdiction to hear and determine all questions respecting the title, possession, or control of the property. In the courts of the United States this ancillary jurisdiction may be exercised, though it is not authorized by any statute. The jurisdiction in such cases arises out of the possession of the property, and is exclusive of the jurisdiction of all other courts, although otherwise the controversy would be cognizable in them. *Wabash R. Co. v. Adelbert College*, 208 U. S. 38, 54. * * * Accordingly, where property was in the possession of the bankrupt at the time of the appointment of a receiver, it was held that the bankruptcy court had jurisdiction to determine the title to it as against an adverse claimant, and that the receiver had no right to deliver it to him without the order of the court. *Whitney v. Wenman*, 198 U. S. 539, 14 Am. B. R. 45. * * * On the day the opinion in the *Bardes* case was announced the same justice delivered the opinion of the court in *White v. Schloerb*, 178 U. S. 542, 4 Am. B. R. 178, * * * a case in which the facts were essentially those of the case at bar. Certain persons, co-partners in trade, were adjudicated bankrupts and the case was sent to a referee in bankruptcy. They had a stock of goods in a store, the entrance to which was locked by the referee. Certain other persons claimed title to part of the stock of goods as obtained from them by a fraudulent purchase, which had been rescinded. After the adjudication, these persons brought an action of replevin of the goods against the bankrupt in a State court, which was executed. It was held that replevin would not lie in the State court, and that the District Court had jurisdiction by summary proceedings to compel the return of the property seized. The court said: 'The goods were then in the lawful possession of and custody of the referee in bankruptcy, and of the bankruptcy court, whose representative and substitute he was. Being thus in the custody of a court of the United States, they could not be taken out of that custody upon any process from a State court.' The last two cases cited proceed upon and establish the principle that when the court of bankruptcy, through the act of its officers, such as referees, receivers, or trustees, has taken possession of a res, as the property of a bankrupt, it has ancillary jurisdiction to hear and determine the adverse claims of strangers to it, and that its possession cannot be disturbed by the process of another court. And see *Skilton v. Codington*, 15 Am. B. R. 810, 185 N. Y. 80, 85, 86, 113 Am. St. Rep. 885, 77 N. E. 790, and *Frank v. Vollkommer*, which, by implication, approve the same principle."

Babbitt v. Dutcher, 216 U. S. 102, 23 A. B. R. 519: "There are two classes

of cases arising under the Act of 1898 and controlled by different principles. The first class is where there is a claim of adverse title to property of the bankrupt based upon a transfer antedating the bankruptcy. The other class is where there is no claim of adverse title based on any transfer prior to the bankruptcy, but where the property is in the physical possession of a third party or of an agent of the bankrupt, or of an officer of a bankrupt corporation, who refuses to deliver it to the trustee in bankruptcy. In the former class of cases a plenary suit must be brought, either at law or in equity, by the trustee, in which the adverse claim of title can be tried and adjudicated. In the latter class it is not necessary to bring a plenary suit, but the bankruptcy court may act summarily and may make an order in a summary proceeding for the delivery of the property to the trustee, without the formality of a formal litigation. The former class falls within the ruling in the case of *Bardes v. Hawarden Bank*, 178 U. S. 524, 4 Am. B. R. 163, and in the case of *Jaquith v. Rowley*, 188 U. S. 620, 9 Am. B. R. 525, which hold that such a suit can be brought only in a court which would have had jurisdiction of a suit by the bankrupt against the adverse claimant, except where the defendant consents to be sued elsewhere. In the latter class of cases a plenary suit is not necessary, but the case falls within the rule laid down in *Bryan v. Bernheimer*, 181 U. S. 188, 5 Am. B. R. 623, and *Mueller v. Nugent*, 184 U. S. 1, 7 Am. B. R. 224, which held that the bankruptcy court could act summarily."

Bank v. Title & Trust Co., 198 U. S. 280, 14 A. B. R. 102 (reversing 11 A. B. R. 79): "The distinction between steps in bankruptcy proceedings proper and controversies arising out of the settlement of the estates of bankrupts is recognized in §§ 23, 24 and 25 of the present Act, and the provisions as to revision in matter of law and appeals were framed and must be construed in view of that distinction. *Holden v. Stratton*, 191 U. S. 115, 10 Am. B. R. 786; *Denver First National Bank v. Klug*, 186 U. S. 202, 8 Am. B. R. 12; *Elliott v. Toeppner*, 187 U. S. 327, 333, 334, 9 Am. B. R. 50.

"This distinction existed under the prior bankruptcy law, and the then decisions in respect of a proceeding in bankruptcy and an independent suit are applicable. It was settled that the bankruptcy court was without jurisdiction to determine adverse claims to property, not in the possession of the assignee in bankruptcy, by summary proceedings, whether absolute title or only a lien was asserted. *Smith v. Mason*, 14 Wall. 419; *Marshall v. Knox*, 16 Wall. 551; *In re Bonesteel*, 7 Blatch. 175, Mr. Justice Nelson; *Knight v. Cheney*, 14 Fed. Cas. 760, Mr. Justice Clifford; *In re Ballow*, 4 Ben. 135, Mr. Justice Blatchford, the district Judge; *In re Marter*, 16 Fed. Cas. 857, Mr. Justice Brown, then district judge.

"The present Act was plainly framed in recognition of the principle of these cases."

Hebert v. Crawford, 228 U. S. 204, 30 A. B. R. 24: "If the rice was then in their possession the bankruptcy court had jurisdiction to administer it as assets of the estate, and to determine all claims to the property. * * * Whatever may have been the legal or equitable rights of the Beaumont Mills under their contracts with Moore & Bridgeman (the bankrupt) and under the bill of sale of June 15, 1906, it still appears that, first, Moore & Bridgeman (the bankrupt) and later LeBlanc, as trustee [in bankruptcy] engaged in gathering, threshing, hauling and delivering the rice. This physical possession, under the decision in *Murphy v. Hofmann Co.*, 211 U. S. 562, 21 A. B. R. 487, gave the bankruptcy court control of the res, and authority to administer it along with all other property in their physical possession when their petition was filed. That petition operated as an attachment and brought the rice into the custody of the bankruptcy court."

Coder v. Arts, 213 U. S. 223, 22 A. B. R. 1: "The Bankruptcy Act, as originally passed, did not give the bankruptcy courts jurisdiction over plenary suits to recover the property alleged to belong to the trustee in bankruptcy, except with the consent of the defendant. This was the subject of full consideration and determination in *Bardes v. First Nat. Bank*, 178 U. S. 524, 4 Am. B. R. 163. * * * Subsequent decisions of this court construed the act to give the bankruptcy courts jurisdiction over controversies concerning the property in possession of the bankruptcy courts."

Inferentially, *Whitney v. Wenman*, 198 U. S. 555, 14 A. B. R. 49: "We think the result of these cases is in view of the broad powers conferred in § 2 of the bankrupt act, authorizing the bankruptcy court to cause the estate of the bankrupts to be collected, reduced to money and distributed, and to determine controversies in relation thereto, and bring in and substitute additional parties when necessary for the complete determination of a matter in controversy, that when the property has become subject to the jurisdiction of the bankruptcy court as that of the bankrupt, whether held by him or for him, jurisdiction exists to determine controversies in relation to the disposition of the same and the extent and character of liens thereon or rights therein."

In *re McMahon*, 17 A. B. R. 531, 147 Fed. 685 (C. C. A. Ohio): "The controlling fact in the matter of the jurisdiction of the bankrupt court is that the actual possession of the premises upon which Enos asserts an adverse lien was in Enos, the trustee in bankruptcy of Campbell, the bankrupt mortgagor. * * * Sec. 2 * * * confers jurisdiction 'to cause the estate of the bankrupt to be collected * * * and determine the controversies in relation thereto, except as herein otherwise provided. This exception refers to § 23 [as to suits brought by trustees]. By the Amendment of February, 1903, this jurisdiction is extended. * * * But we are now dealing with the jurisdiction of the District Court which had possession through its trustee of the property of the bankrupt, against which the protesting petitioner asserts a mortgage lien. If the District Court, having possession of the res, did not have jurisdiction to hear and determine claims to or against the res, unless the claimant should consent, what court did? Could the petitioner go into the State court and there assert his lien, and then obtain a decree for its enforcement, and thus deprive the court of primary jurisdiction of the control and custody of the controverted property?"

"The possession of the res draws to the court jurisdiction of all questions in respect to title or liens, irrespective of citizenship.

"What is said in *Bardes v. Hawarden Bank* about the absence of intention of Congress to give under § 2, clauses 6 and 7, jurisdiction to the District Court to entertain independent actions and suits to determine the title to property or liens thereon, refers to property not held by the bankrupt or some one for him at the date of adjudication."

Odell v. Boyden, 17 A. B. R. 756, 150 Fed. 731 (C. C. A. Ohio): "* * * there exists no ground for entertaining jurisdiction to adjudicate his claim or lien unless we shall agree with the court below in holding that the 'membership' or 'seat' was an asset which passed to the trustee and was in custodia legis when the petition was filed."

Loeser v. Bank & Trust Co., 20 A. B. R. 845, 163 Fed. 212 (C. C. A. Ohio): "It involved the claim of the bank under a chattel mortgage to assets in the possession of the bankrupt's trustee. The bankrupt court, under the broad powers conferred by § 2 of the Bankruptcy Act, had the power to determine controversies relating to the estate of the bankrupt in its possession, whether

the controversy related to the title or to liens thereon or rights therein. The property here involved had been surrendered by the bank to the trustee; the bank reserving its rights against the proceeds of sale. Having the actual possession, it mattered nothing whether the trustee instituted a proceeding to bring the bank in for the determination of the controversy, or whether the bank had intervened by petition to assert its rights."

In *re Grassler v. Reichwald*, 18 A. B. R. 694, 154 Fed. 478 (C. C. Calif.): "The only question, therefore, presented for our consideration on this petition is whether the proper remedy of the trustee to recover the money which was obtained by the petitioner was a plenary suit in court or a summary proceeding such as he adopted. If the property had been in the adverse possession of the petitioner before the bankrupts filed their petition to be adjudicated bankrupts there can be no doubt that a plenary suit would have been necessary. But assuming, as we may under the record, the facts to have been, as it is claimed by the respondent herein that they were, that certain property of the bankrupts was taken upon void attachment and that the money realized on the sale thereof was paid to the petitioner on a judgment entered in his favor by default against the bankrupts several weeks after they had filed their petition in the District Court to be adjudicated bankrupts, and that this was known to the petitioner, we think there can be no question that under the provisions of § 2 (7) and § 67f of the Bankruptcy Act, authorizing the referee to compel the surrender of funds to the trustee, the proceeding had before the referee in this case was permissible. *Bryan v. Bernheimer*, 181 U. S. 185, 5 Am. B. R. 523; *Mueller v. Nugent*, 184 U. S. 1, 7 Am. B. R. 224; In *re Breslauer* (D. C.), 10 Am. B. R. 33, 121 Fed. 910; In *re Goldberg* (D. C.), 10 Am. B. R. 97, 121 Fed. 578. And, if the referee could lawfully make the order, it follows that the court below could deal with the petitioner as for contempt, and commit him to imprisonment for refusal to obey the order."

In *re Epstein*, 19 A. B. R. 89, 156 Fed. 42 (C. C. A. Colo.): "A court of bankruptcy, may by summary process, require those who assert title to, or an interest in, property which was rightfully come into its possession and control as part of the bankrupt's estate, to present their claims to that court, and, the notice being reasonable, may proceed to adjudicate the merits of such claims."

Johnston v. Spencer, 27 A. B. R. 805, 195 Fed. 215 (C. C. A. Colo.): "According to these controlling decisions the possession of property by the bankrupt at the time of the institution of the proceedings in bankruptcy, is a necessary condition to jurisdiction in the District Court to determine the rights of third parties to it except when such jurisdiction is invoked by their consent. The possession may be in the bankrupt himself or by someone for him as his agent or bailee."

Mound Mines Co. v. Hawthorne, 23 A. B. R. 242, 173 Fed. 882 (C. C. A. Colo.): "The law is now settled that the interest of a third party in property claimed to belong to the bankrupt estate, which, at the time of the institution of the proceedings in bankruptcy, is in the possession of such third person, claiming an interest therein, can only be determined by an original suit brought for that purpose. Where, however, property which is in the possession of a bankrupt at the time of the bankruptcy proceedings, and passes as part of his estate into the possession of the trustee in bankruptcy, and a third party claims an interest therein, the referee may, by a summary proceeding, require such third party to appear in the bankruptcy court, present his claim, and the referee adjudicate the rights of the parties in respect thereof."

In *re Baudouine*, 3 A. B. R. 651, 191 Fed. 574 (C. C. A. N. Y.): "Standing

alone, the language of clause 7 would seem to be sufficiently comprehensive to authorize the determination by Courts of Bankruptcy of every controversy relating to the estates of bankrupts. * * * Nevertheless, it is capable of a narrower construction, and can be read as extending only to controversies about property which actually belongs to the bankrupt's estate, or which arise strictly in the bankruptcy proceeding, such as those in reference to the marshaling of assets, or the extent and priority of conflicting liens."

In *re Kellogg*, 10 A. B. R. 7, 121 Fed. 333 (C. C. A. N. Y., affirming 7 A. B. R. 623): "It would seem that the controversies in relation to the bankrupt estate, which, by reason of the limitations referred to in the clause 'except as herein otherwise provided,' do not come within the jurisdiction of the bankruptcy courts, are those where the trustee must bring an independent suit to assert title to money or property not in the possession or control of the trustee."

In *re Andre*, 13 A. B. R. 132 (C. C. A. N. Y.): "We conclude that it is only in cases in which the property of the bankrupt is in the possession of a party not an adverse claimant that the courts of bankruptcy have authority under these sections to interfere with it unless the adverse claimant chooses to consent, but that these courts have jurisdiction to entertain proceedings to ascertain whether there is an adverse claimant and that the mere refusal of a person in possession to surrender the property does not constitute him an adverse claimant."

Inferentially and obiter, In *re Bacon*, 20 A. B. R. 107, 159 Fed. 424 (C. C. A. N. Y.): "The property in question was in the actual custody of the trustee, having been turned over to him by the bankrupt himself, when the claim of title was examined into. Having elected to go on with such examination without taking any steps to review the orders under which it was conducted, petitioner [the bankrupt's wife] cannot now be heard to question the jurisdiction. If consent were necessary to give jurisdiction, such consent will be inferred from the circumstances that she proceeded under the order of July 15, 1905, without seeking to review it. In disposing of the case on this ground, however, we are not to be understood as expressing the opinion that such consent was necessary. The situation of the case as presented, renders it unnecessary to decide that question, to which the briefs and arguments were mainly addressed."

In *re Brooks*, 1 A. B. R. 531, 91 Fed. 508 (D. C. Vt.): "In this case the court held in substance that the mortgagee of chattels has no right to foreclose a mortgage upon the chattels of a bankrupt unless he obtains permission of the Court of Bankruptcy in which the petition is filed, or unless some action is commenced to make such foreclosure in a State court and such court gets jurisdiction over such chattels, or unless the mortgagee or the officer making such sale gets exclusive possession of the chattels before the adjudication in bankruptcy."

In *re Rose Shoe Mfg. Co.*, 21 A. B. R. 725, 168 Fed. 39 (C. C. N. Y.): "It is clear the returned merchandise came into the actual possession of the receiver as a part of the bankrupt's property. * * * And being in the custody of the receiver the merchandise was in the possession of the bankruptcy court which had the right when such possession was disturbed, to regain it by summary proceedings and to adjudicate with respect to all claims concerning the property."

In *re Leeds Woolen Mills*, 12 A. B. R. 136 (D. C. Tenn., reversed, on the facts, in *Hinds v. Moore*, 14 A. B. R. 1): "The facts pertinent to the element of jurisdiction are that at the time of the bankruptcy the goods in contro-

versy were in the actual manual possession of the bankrupt corporation and passed from it into the manual possession of the referee as custodian, upon the surrender of these and all the other goods to him. In my judgment, the simple fact of this possession by the referee in bankruptcy is conclusive in favor of our jurisdiction. By that possession the goods were in custodia legis—whether rightfully or wrongfully, is another question. But that question may be rightfully decided by us. Whether it might also be rightfully decided by any other jurisdiction it is not necessary to determine. The bare possession by the court, through its officers, of the property, was sufficient to give us jurisdiction to determine to whom the goods properly belonged. The case belongs to the category of those controlled by the decision of the Supreme Court of the United States in the case of *White v. Schloerb*, 178 U. S. 542, 4 Am. B. R. 178, and not to that of those controlled by the decision of that court in *Bardes v. Hawarden Bank*, 178 U. S. 524, 4 Am. B. R. 163.”

In *re Lemmon & Gale*, 7 A. B. R. 291, 112 Fed. 296 (C. C. A. Tenn.): “This property was, consequently in the possession of the court when undertaken to be levied upon by the sheriff executing process issued upon the judgments rendered in the State court. In view of this situation the bankruptcy court undoubtedly had jurisdiction to determine the rights of others asserting a lien upon or interest in the property, and the property could not be taken from the control of the bankruptcy court by the process of the State court.
* * *

“The United States Court having lawful possession of the res, might retain it until it had disposed of the property.”

In *re Lines*, 13 A. B. R. 318, 133 Fed. 803 (D. C. Pa.): “It is undisputed that after the distress had been made, title to the goods, which was then in Mrs. Fannie Dryden, was transferred by her to her father, John M. Lines, the present bankrupt, and that he immediately filed a voluntary petition and was adjudged a bankrupt. The necessary effect of this was to put the property under the control of this court, and compel the landlord to seek redress here.”

In *re Noel*, 14 A. B. R. 720, 137 Fed. 694 (D. C. Md.): “I think the distinction between the controversies arising in bankruptcy which must be determined by plenary independent suits and those which may be heard on summary petition depends upon who has possession of the subject matter of the controversy. If the bankruptcy court has possession, then, as a rule, the matter may be heard upon petition and answer. If a stranger has possession, and is holding by adverse claim, then an independent plenary suit is in most cases proper. In this case, the property was in the possession of the bankrupt, and upon his adjudication his title and possession passed to the trustees. The possession of the trustees could not be disturbed by any form of adverse legal proceedings without the concurrent sanction of the court of bankruptcy. That court, having possession of the property, had jurisdiction, upon notice to those claiming to have liens and incumbrances upon it, to order the property to be sold by the trustees free of all incumbrances, if the court, in its discretion, should determine that such a sale was for the benefit of the unsecured creditors; and after such a sale, having in its control the fund arising from the sale, it would have jurisdiction to determine the conflicting claims of the parties whose liens had been displaced as to the property sold, and transferred to the fund in the court. *Ray v. Norseworthy*, 23 Wall. 128, 23 L. Ed. 116.”

Obiter, impliedly, In *re Hadden-Rodee Co.*, 13 A. B. R. 605, 135 Fed. 886 (D. C. Wis.): “Questions of the power to entertain summary proceedings

against adverse claimants of property have frequently arisen, and the doctrine is settled that such proceedings are authorized only when the property is in the possession of the court, or in cases wherein the statute so provides in express terms."

Plaut, Trustee, v. Gorham Mfg. Co., 20 A. B. R. 269, 159 Fed. 754 (D. C. N. Y.): "The complaint alleges that the receiver occupied the premises for the month of August, 1906, and that the defendant, the Gorham Mfg. Co. wrongfully dispossessed him in September, under a dispossession warrant issued by a magistrate without jurisdiction, and has since been in possession. I think that these allegations show that this court has jurisdiction. I understand the test to be whether the property is or has been in the possession of an officer of the bankruptcy court. If it is in such possession, claimants can be cited into the bankruptcy court to determine the validity of any claims or liens asserted against it. In *re Rochford*, 10 Am. B. R. 608, 124 Fed. 182; In *re Kellogg*, 10 Am. B. R. 7, 121 Fed. 333; In *re Epstein*, 19 Am. B. R. 89, 156 Fed. 42. If it has been in such possession and has been wrongfully withdrawn from such possession, suits may be brought in the bankruptcy court to recover it. *Whitney v. Wenman*, 198 U. S. 539, 14 Am. B. R. 45. It is in the cases where property claimed to belong to the bankrupt is and always has been in the possession of another party that this court has no jurisdiction, as held in *Bardes v. Bank*, 178 U. S. 524, 4 Am. B. R. 163, unless the property has been fraudulently or preferentially transferred as provided for in the amendments of the Bankrupt Act in 1903."

Obiter, In *re Walsh Bros.*, 21 A. B. R. 14, 163 Fed. 352 (D. C. Iowa): "* * * where the court has acquired possession in the course of such proceedings * * * the power inheres in the court of bankruptcy, as in every court exercising equitable jurisdiction to inquire and determine in a proper way the ownership of or right to the property in its custody, and award it accordingly, and this, though the property may have been wrongfully seized and brought into its custody." Quoted further at § 1652.

And it has been held that jurisdiction attaches to this end even though the property has been wrongfully seized and brought into custody.³

Even where the state court had taken possession of property, real estate, by its receiver, before bankruptcy, in a foreclosure suit, and where there was no claim made of a preferential transfer or any invalidity of liens for other causes, yet the state court receiver having voluntarily surrendered possession, the bankruptcy court was held, on indisputable grounds, to have complete jurisdiction to marshal liens and determine all rights of parties, even to the extent of enjoining the further prosecution of the foreclosure suit itself.

In *re Dana*, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.): "The principal question arising on this petition to revise is whether a District Court of the United States, in which proceedings in bankruptcy are pending, and which is in the actual possession of certain real property conceded to belong to the bankrupt, has jurisdiction to determine the amount and the order of priority of liens thereon, and to liquidate such liens, to the end that the property may be sold free of incumbrances, and in aid thereof to enjoin the lienholders

3. Obiter, In *re Walsh Bros.*, 21 A. B. R. 14, 163 Fed. 352 (D. C. Iowa), quoted at § 1796, citing *Krippendorff v. Hyde*, 110 U. S. 276; obiter, In *re Moody*, 12 A. B. R. 724, 131 Fed. 525 (D. C. Iowa), quoted at § 1797.

from prosecuting the foreclosure of their liens in a suit brought in a State court before the commencement of the bankruptcy proceedings, but within four months thereof; and this, though the lienholders object to such jurisdiction, and it is not contended that their liens are preferential or fraudulent, or invalid for any other reason. Bearing in mind the property was the property of the bankrupt, the title to which had passed to the trustee in bankruptcy, and that it was in the actual possession of the District Court of the United States, we think an affirmative answer should be given upon the authority of *In re Schermerhorn* [quoted supra]; *In re Epstein*, 19 A. B. R. 89, et seq. * * * Indeed, it appears that before the injunction in question was awarded, the State court, which by its receiver had actual possession of the property, voluntarily surrendered it to the receiver appointed in the bankruptcy proceedings upon request being made."

DIVISION 1.

SUMMARY JURISDICTION OF BANKRUPTCY COURT, IN GENERAL.

§ 1797. Jurisdiction Once Attaching, Complete for All Purposes.—After the bankruptcy court has once assumed jurisdiction over the property, it has jurisdiction to determine all rights therein.⁴

White v. Schloerb, 178 U. S. 542, 4 A. B. R. 178: "At the date of this adjudication in bankruptcy by the District Court of the United States, the goods

4. Compare, ante, "Restraining Orders before Adjudication," § 359, and post, "Restraining Orders and Injunctions in Aid of Bankruptcy Proceedings," § 1901.

Bankr. Act, § 2 (7): "Cause the estates of bankrupts to be collected reduced to money and distributed, and determine controversies in relation thereto, except as herein otherwise provided."

Salsburg v. Blackford, 29 A. B. R. 320, 204 Fed. 438 (C. C. A. W. Va.); *LeMaster v. Spencer*, 29 A. B. R. 264, 203 Fed. 210 (C. C. A. Colo.), quoted at § 1798; obiter, *In re Baudouine*, 3 A. B. R. 651, 91 Fed. 574 (C. C. A. N. Y.); *In re Emslie*, 4 A. B. R. 126, 102 Fed. 291 (C. C. A. N. Y.); *In re Noel*, 14 A. B. R. 720, 137 Fed. 694 (D. C. Md.); *In re Huddleston*, 1 A. B. R. 572 (Ref. Ala.); *In re Granite City Bk.*, 14 A. B. R. 404, 137 Fed. 818 (C. C. A. Iowa); [1867] *Freeman v. Howe*, 24 How. 450; [1867] *Bank v. Sherman*, 101 U. S. 406; [1841] *Buck v. Calhath*, 3 Wall. 341; *Treat v. Wooden*, 14 A. B. R. 736 (C. C. Mass.); *In re Schloerb*, 3 A. B. R. 224 (D. C. Wis., affirmed sub nom. *White v. Schloerb*, 4 A. B. R. 178, 178 U. S. 542); inferentially, *Havens & Geddes Co. v. Pierek*, 9 A. B. R. 569, 120 Fed. 244 (C. C. A. Ills.); *In re J. C. Winship Co.*, 9 A. B. R. 641, 120 Fed. 93 (C. C. A. Ills.); *In re Russell & Birkett*, 3 A.

B. R. 658, 101 Fed. 248 (C. C. A. N. Y., distinguished in *In re Spitzer*, 12 A. B. R. 346, 130 Fed. 879, and in *In re Kantor & Cohen*, 9 A. B. R. 372, 121 Fed. 984); inferentially, *In re New England Piano Co.*, 9 A. B. R. 767, 122 Fed. 937 (C. C. A. Mass.); *In re Lemmon & Gale Co.*, 7 A. B. R. 291, 112 Fed. 96 (C. C. A. Tenn.), quoted previously, § 1794; *In re Kellogg*, 7 A. B. R. 631, 113 Fed. 190 (D. C. N. Y., affirmed in 10 A. B. R. 7); *In re Renda*, 17 A. B. R. 522, 149 Fed. 614 (D. C. Penn.); *Carriage Co. v. Solanas*, 6 A. B. R. 221, 108 Fed. 532 (D. C. La.); *In re Chambers, Calder & Co.*, 3 A. B. R. 537, 98 Fed. 865 (D. C. R. I.); *Odell v. Boyden*, 17 A. B. R. 756, 150 Fed. 731 (C. C. A. Ohio); impliedly, *In re Kleinhans*, 7 A. B. R. 607, 113 Fed. 107 (D. C. N. Y.); impliedly, *In re Hymes Buggy & Implement Co.*, 12 A. B. R. 477, 130 Fed. 977 (D. C. Mo.); *In re Leeds Woolen Mills Co.*, 12 A. B. R. 136 (reversed, on facts, in *Hinds v. Moore*, 14 A. B. R. 1, C. C. A. Tenn.); *In re Lumber Co. (Franklin)*, 17 A. B. R. 446, 147 Fed. 852 (D. C. N. J.); *In re Ludowici Roofing Tile Co. v. Penn. Inst.*, 8 A. B. R. 742 (D. C. Penn.); obiter, *Hinds v. Moore*, 14 A. B. R. 1 (C. C. A. Tenn., reversing, on facts, *In re Leeds Woolen Mills Co.*, 12 A. B. R. 136); obiter, *In re Corbett*, 5 A. B. R. 224, 104 Fed. 872 (D. C. Wis.); obiter, *In re Wells*,

were in the store of the bankrupts, and in their actual possession, and were claimed by them as their property. On the same date, that court referred the case to a referee in bankruptcy, and by his direction the entrance to the store was locked. The goods were then in the lawful possession and custody of the referee in bankruptcy, and of the bankruptcy court, whose representative and substitute he was. Being thus in the custody of a court of the United States, they could not be taken out of that custody upon any process from a State court. * * * 'After an adjudication in bankruptcy, an action in replevin in a State court cannot be commenced and maintained against the bankrupt to recover property in the possession of and claimed by the bankrupt at the time of that adjudication, and in the possession of a referee in bankruptcy at the time when the action of replevin is begun.' * * *

"Not going beyond what the decision of the case before us requires, we are of the opinion that the judge of the court of bankruptcy was authorized to compel persons, who had forcibly and unlawfully seized and taken out of the judicial custody of that court property which had lawfully come into its possession as part of the bankrupt's property, to restore that property to its custody; and therefore our answer to the first question must be: 'The District Court sitting in bankruptcy had jurisdiction by summary proceedings to compel the return of the property seized.'"

Murphy v. John Hofman Co., 211 U. S. 562, 21 A. B. R. 487: "When the court of bankruptcy, through the act of its officers, such as referees, receivers or trustees, has taken possession of a res, as the property of the bankrupt, it has ancillary jurisdiction to hear and determine the adverse claims of strangers to it and its possession cannot be disturbed by the process of another court."

Compare, *Whitney v. Wenman*, 198 U. S. 539, 14 A. B. R. 45: "This case holds, not that the action must be taken in the bankruptcy court, for that issue was not raised nor necessary to be determined, but rather that the bankruptcy court possessed jurisdiction. See the opinion of the court on page 51:

"We think the result of these cases is, in view of the broad powers conferred in § 2 of the Bankrupt Act, authorizing the bankruptcy court to cause the estate of the bankrupt to be collected, reduced to money and distributed, and to determine controversies in relation thereto, and bring in and substitute additional parties when necessary for the complete determination of a matter in controversy, that when the property has become subject to the jurisdiction of the bankruptcy court as that of the bankrupt, whether held by him or for him, jurisdiction exists to determine controversies in relation to the disposition of the same and the extent and character of liens thereon or rights therein."

In *re Whitener*, 5 A. B. R. 198, 105 Fed. 180 (C. C. A. Tex.): "As the property, the ownership of which is in dispute, was in the possession of the

8 A. B. R. 76, 114 Fed. 222 (D. C. Mo.); *Traders' Ins. Co. v. Mann*, 11 A. B. R. 269 (Sup. Ct. Ga.); *Goodnough Mercantile & Stock Co. v. Galloway*, 19 A. B. R. 244, 156 Fed. 504 (D. C. Ore.); In *re Bacon*, 20 A. B. R. 107, 159 Fed. 424 (C. C. A. N. Y.); *Plaut v. Gorham Mfg. Co.*, 20 A. B. R. 269, 159 Fed. 754 (D. C. N. Y.), quoted at § 1796; impliedly, *Knapp & Spencer Co. v. Drew*, 20 A. B. R. 355, 160 Fed. 413 (C. C. A. Neb.); impliedly, In *re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa), quoted at § 1488½; *Cleminshaw v. Shirt & Collar Co.*, 21 A. B. R. 616, 165 Fed.

797 (D. C. N. Y.); In *re Dana*, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.), quoted at § 1796; impliedly, *Graphophone Co. v. Leeds & Catlin Co.*, 23 A. B. R. 337, 174 Fed. 158 (C. C. N. Y.), quoted post, § 1806¼; In *re MacDougall*, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.); In *re New England Breeders' Club*, 23 A. B. R. 689, 175 Fed. 501 (D. C. N. H.); *Chism v. Bank*, 5 A. B. R. 56, 77 Miss. 599, wherein the court held it to be incident to the trustee's rights and duties. Impliedly, In *re Zehner*, 27 A. B. R. 536, 193 Fed. 787 (D. C. La.).

trustee in bankruptcy as a part of the bankrupt's property to be duly administered, the District Court had jurisdiction to issue an injunction restraining the proceedings under a sequestration issued from the District Court of Bowie County, Texas, at the suit of Ramseur, plaintiff, against Rodgers, trustee, and to compel the return of the property to the trustee. * * * The property being in the custody of the District Court sitting in bankruptcy, that court had jurisdiction to entertain the intervention filed by Ramseur, claiming the property, and to hear and determine the issues presented by the intervention, not only on general principles, * * * but under the specific provisions of § 2 of the Bankruptcy Act of 1898."

In re Epstein, 19 A. B. R. 89, 156 Fed. 42 (C. C. A. Colo.): "The question of jurisdiction is not free from doubt but we are of opinion that the result of the cases is that a court of bankruptcy may by summary process require those who assert title to or an interest in, property which has rightfully come into its possession and control as part of the bankrupt's estate to present their claims to that court, and, the notice being reasonable, may proceed to adjudicate the merits of such claims."

In re Antigo Screen & Door Co., 10 A. B. R. 359, 123 Fed. 249 (C. C. A. Wis.): "We take it that any court, whether one of equity, common law, admiralty or bankruptcy, having in its treasury a fund touching which there is dispute, may, by virtue of its inherent powers, determine the right to the fund thus in its possession. Jurisdiction in that respect is an incident of every court. * * * A fund so possessed, is in custodia legis and right to it may only be asserted and determined in the court which possesses it."

In Rodgers, 11 A. B. R. 89, 125 Fed. 169 (C. C. A. Ills. reversed on facts sub nom. First Nat'l Bk. v. Chic Title & T. Co., 14 A. B. R. 102, 198 U. S. 280): "The court below properly ruled that it had jurisdiction of the subject matter. Its officers acquired possession of the property in dispute from the bankrupt. It is, indeed, claimed by the storage company that the writings and the facts embodied in the statement of the case show that it, and not the bankrupt, had possession prior to the bankruptcy; but the receiver had in fact acquired peaceable possession of the property, and subsequent proceedings in the bankruptcy court upon petition of the present objectors to the jurisdiction, by which the property was sold by the bank under stipulation that it should hold the fund subject to the order of the court, placed the property and its proceeds in custodia legis, and the court had the right to determine the ownership of the fund in its possession."

In re Schermerhorn, 16 A. B. R. 508, 145 Fed. 341 (C. C. A.): "Upon the filing of a petition in bankruptcy, followed by an adjudication, all property in the possession of the bankrupt of which he claims the ownership passes at once into the custody of the court of bankruptcy, and becomes subject to its jurisdiction to determine by plenary action or summary proceedings, as the nature of the case demands, all adverse or conflicting claims thereto whether of title or of lien, and that court may, by the process of injunction, protect its jurisdiction against interference. It may draw to itself the determination of all controversies over the property in its possession, and when it once lawfully attaches, its jurisdiction cannot be destroyed or impaired by the unauthorized surrender of possession of the property by the officers of the court or through a seizure thereof by any adverse claimant."

In re Kellogg, 10 A. B. R. 7, 121 Fed. 333 (C. C. A. N. Y., affirming 7 A. B. R. 623, 113 Fed. 190): "The final question is whether the Supreme Court of the State of New York acquired jurisdiction of the property, to the exclusion of the United States District Court, by the filing of the summons, com-

plaint, and notice of pendency of the foreclosure action, before the trustee was appointed; the bankruptcy court having previously acquired jurisdiction by the filing of the petition in bankruptcy and the appointment of a receiver, who had qualified and taken possession of the property prior to the commencement of said action and foreclosure * * * The court in the foreclosure suit had not attempted to take possession. The adjudication was equivalent to the commencement of an action and the filing of a *lis pendens*. It must be held that the bankruptcy court, upon such acquisition by the receiver of possession and undisputed legal title, had jurisdiction to determine the validity of the mortgage."

In *re Rochford*, 10 A. B. R. 615, 124 Fed. 182 (C. C. A. S. Dak.): "In the case in hand the court below lawfully acquired the possession of the mortgaged goods, and it lawfully converted them into money. The rightful custody of the property and its proceeds imposed upon that court the duty to distribute the latter to their true owners. This possession and this duty necessarily empowered it to call the petitioners by a notice or order to show cause to present their claims to the property or its proceeds to the court which held them within a reasonable time, or to be barred of any right to receive the property or the proceeds or any part of either."

Chauncey v. Dyke Bros., 9 A. B. R. 447, 119 Fed. 1, 3 (C. C. A. Ark.): "A court which has lawfully acquired the custody of property or money must of necessity dispose of the same according to law; and, when conflicting claims are preferred, it is not bound to require the claimants to litigate their claims in some other forum, and to adopt the judgment of that tribunal, although it may do so, but it is at liberty to dispose of such controversies according to its own ideas of right and justice. This is one of those incidental powers which may be exercised by any court of record in the absence of an express prohibition."

Turrentine v. Blackwood, 4 A. B. R. 338, 28 So. 95 (Sup. Ct. Ala.): "Conceding that the State and Federal courts have concurrent jurisdiction in certain instances over the bankrupt's property, another principle is universally acknowledged, 'that when two courts have concurrent jurisdiction, that which first takes cognizance of the case, has the right to retain it, to the exclusion of the other; that if a trust estate is being administered by a court of competent jurisdiction, or when property is in *gremio legis* of a court of rightful jurisdiction, no other court can interfere and wrest from it the possession and jurisdiction first obtained.'"

In *re Drayton*, 13 A. B. R. 602, 135 Fed. 883 (D. C. Wis.): "The property or proceeds in question in the present case is in the hands of the trustee, in *custodia legis*, and the Bankruptcy Court is necessarily vested with both power and duty to determine all rights therein, upon proper notice, as 'controversies in relation thereto.' * * *

"It would be anomalous indeed if the Act were interpreted to deprive the tribunal of such jurisdiction as a court of bankruptcy in possession of the res."

Carter v. Hobbs, 1 A. B. R. 215, 92 Fed. 594 (D. C. Ind.): "The decree operates in rem and from the moment of the adjudication of bankruptcy the bankrupt's estate is in *custodia legis* and under the jurisdiction of this court. It is fundamental that no court or individual can interfere with such custody and possession. The assertion of any right against, or to participate in, the res so in *custodia legis*, must be sought in the court in whose custody it is. An attempt to assert such right elsewhere would be regarded as a contempt.

"The adjudication proceeds in rem, and all persons interested in the res are

regarded as parties to the bankruptcy proceeding. These parties include not only the bankrupt and trustee, but also all the creditors of the bankrupt."

In *re Cobb*, 3 A. B. R. 130, 96 Fed. 821 (D. C. Car., reversed, on other grounds, in *Cobb v. Overman*, 6 A. B. R. 324, 109 Fed. 65): "After an adjudication in bankruptcy, the bankrupt court takes jurisdiction of the estate and all matters pertaining thereto, and will administer the same to a final settlement. Parties having or claiming an interest in the bankrupt estate must submit them to the bankruptcy court. * * * The trustee is vested by law with the estate, and could, by a proper action, recover possession of the securities in possession of any one as collateral, subject to any valid lien such person might have on the proceeds of such securities."

In *re Reynolds*, 11 A. B. R. 758, 127 Fed. 760 (D. C. Mont.): "In virtue of the adjudication of bankruptcy, this court acquired jurisdiction over the res. The jurisdiction thus acquired was both complete and exclusive. Being prior to that of the State court, it was permanent. The State court was without jurisdiction in the premises, and any judgment it may have rendered as a result of the litigation between Strain and said trustee, it was and is powerless to enforce, and is not binding upon this court; and such judgment cannot affect the right and power of this court to assert its jurisdiction over the property in question, and proceed to a determination of the right to its possession. * * *

"An adjudication of bankruptcy operates in rem, and from the moment of the adjudication the bankrupt's estate is under the jurisdiction of the bankruptcy court, which will not permit any interference with its possession, even though it be by an officer of a State court acting under its process. Being a proceeding in rem, all parties interested in the res are regarded as parties thereto, including the bankrupt and trustee, as well as the creditors secured and unsecured. The adjudication vests in the trustee or temporary receiver the title of the bankrupt's property, and stays all seizures made within four months. An adjudication of bankruptcy has the force and effect of an attachment and an injunction. It is a caveat to all the world."

In *re Brooks*, 1 A. B. R. 531, 91 Fed. 508 (D. C. Vt.): In this case a chattel mortgagee sold chattels of the bankrupt through a constable who had levied on the same before the bankruptcy, but had left them locked up on the bankrupt's premises. The court said: "But the assets of the bankrupt are brought by the proceedings within the reach and control, and subject to the orders, of the court, and no one has any right to remove or meddle with them, but for their preservation, without leave of the court, except the trustee."

In *re McCallum*, 7 A. B. R. 596, 113 Fed. 393 (D. C. Penn.): "It seems to me, that the present application is the ordinary case of a claim against a fund in the hands of a court, and such claims the court in possession of the fund has the right to hear and determine. It is an incident to the power to distribute, and, except where this power is expressly so limited by competent authority that a claim to a share of the fund must be sent to some other court for determination, the court that has possession of the fund is the proper tribunal to decide all controversies concerning its ownership."

Keegan v. King, 3 A. B. R. 79, 96 Fed. 758 (D. C. Ind.): "After this court has taken actual possession of property, through its receiver and trustee, as the property of the bankrupt, and has retained the actual and continuous possession of the same from a time long anterior to the commencement of the suit in the State court, is it competent for parties who claim to be the owners of the property so in the actual custody and possession of this court to maintain a suit in the State court for the purpose of setting the title and enjoining the officer of this court from the proceeding to the disposition of property so

in the actual possession of this court? The statement of the question would seem to carry its own answer. This court, being in the actual possession of the property in controversy, has the exclusive right to determine all conflicting claims as to the title and right of possession of the property so in its custody. * * * From the time such property, by the adjudication of bankruptcy, comes into the custody of the Bankruptcy Court, it is in custodia legis; and that court will not permit any person, even though he be an officer of a State court, acting under its process, to interfere with the custody or possession by the Bankruptcy Court or its officers of the property thus in its custody."

Inferentially, *In re Moody*, 12 A. B. R. 724, 131 Fed. 525 (D. C. Iowa): "It is a familiar principle of equity jurisprudence that property in the custody of a court of equity is always held by it in trust for those to whom it rightly belongs; and the jurisdiction to inquire into and determine to whom it so belongs, and to that end to require all claimants thereto to present their claims within a stated time, or be barred of any interest in or right to the property, is inherent in every court in equity. *In re Rochford* (C. C.), 10 Am. B. R. 608, 124 Fed. 187, above. And this though the property may have been wrongfully seized, and so brought into the custody of the court."

Crosby v. Spear, 11 A. B. R. 613, 98 Me. 542: "When a court, State or Federal, has once taken into its jurisdiction a specific thing, no court, except one having a supervisory control or superior jurisdiction in the premises has a right to interfere with and change that possession."

In re Porterfield, 15 A. B. R. 18, 138 Fed. 192 (D. C. W. Va., reversed sub. nom. *Moore v. Green*, 16 A. B. R. 607, 145 Fed. 480, C. C. A., on question as to whether State laws regarding priorities on setting aside of transfers should control in bankruptcy): "The jurisdiction of the bankrupt court is exclusive, at least when fully and rightfully obtained over the property itself, as held in such cases as *In re Watts* (10 A. B. R. 113, 190 U. S. 1); and all State laws for the administration of insolvent estates, and all actions and proceedings under such laws, under such circumstances, are suspended."

In re McBride & Co., 12 A. B. R. 83, 132 Fed. 285 (Ref. N. Y.): "The jurisdiction conferred on courts of bankruptcy of § 2, subdivision 7, of the Act over bankrupt estates, 'to determine all controversies in relation thereto,' is applicable to proceedings of this nature, where the property is actually in the possession of the court or its officers, and is subject to distribution under its directions."

In re Mertens, 12 A. B. R. 698, 131 Fed. 972 (D. C. N. Y.): "When property sold to the bankrupt prior to proceedings in bankruptcy is found in his possession, mingled with his stock in trade or other property, it is presumably his, and when the bankruptcy court has taken possession of it and assumed control through its duly appointed receiver before a rescission of the sale, the vendor who assumes thereafter to rescind the sale on the ground of fraud practiced by the vendee (now the bankrupt), and who seeks to recover the property, or its proceeds, or damages from such officer of the court who has held and sold it pursuant to the order of the court, should be compelled to come into the court having the possession and control of the property, and try the question of title thereto there, unless that court is without jurisdiction to try the question, or the law of the United States has expressly placed concurrent jurisdiction elsewhere. If the court should find that the sale was procured by fraud, then the rescission would be valid, and the title would be in the vendor, and he would be entitled to the property, or its value, from the estate of the bankrupt, and this court would so award; but should the court find that such sale was not procured by fraud, then the rescission would be

of no avail, and the title would be in the trustee in bankruptcy when appointed."

In re Sentence & Green Co., 9 A. B. R. 649, 120 Fed. 436 (D. C. N. Y.): "As the property has been taken by the court, and is now subject to its control and direction, it has, upon the alleged lienor's application, power to determine the question of the mortgage lien, notwithstanding the objection of the trustee."

In re Lines, 13 A. B. R. 319, 133 Fed. 803 (D. C. Pa.): "He immediately filed a voluntary petition and was adjudged a bankrupt. The necessary effect of this was to put the property under the control of this court and compel the landlord to seek redress here."

In re Pittelkow, 1 A. B. R. 473, 92 Fed. 901 (D. C. Wis.): "Upon the general question of jurisdiction, I am of opinion that the District Court is vested with exclusive jurisdiction over the property of the bankrupt, and with sufficient equity powers to have all claims by mortgagees brought in and administered; that sales may be authorized, under proper circumstances, free and clear from the mortgages, or other liens, by preserving and transferring the claims to the fund thus provided; and that the commencement of foreclosure proceedings can be restrained to that end."

But in some cases it has been held that if it once determines the right of possession to be in an adverse claimant, the bankruptcy court is without jurisdiction to order distribution, and may only order surrender to such claimant.⁵ And the bankruptcy court is to determine whether its jurisdiction exists.⁶

§ 1798. All Action to Be Taken in Bankruptcy Court.—And all action in regard to property in its custody must be taken (unless, perhaps, in some cases, the bankruptcy court permits otherwise) in the bankruptcy court.⁷

5. In re Smyth, 21 A. B. R. 853, 167 Fed. 871 (D. C. Pa.). Compare similar rule, § 1032.

6. Hebert v. Crawford, 228 U. S. 204, 30 A. B. R. 24: "But it [the state court] could not determine who was in possession of the rice on July 16, 1906, nor who was entitled to the property or its proceeds."

7. Hebert v. Crawford, 228 U. S. 204, 30 A. B. R. 24, quoted at § 1807; White v. Schloerb, 4 A. B. R. 178, 178 U. S. 542; In re McCallum, 7 A. B. R. 596, 113 Fed. 393 (D. C. Penn.); inferentially, In re Briskman, 13 A. B. R. 58, 132 Fed. 201 (D. C. N. Y.); In re Whitener, 5 A. B. R. 198, 105 Fed. 180 (C. C. A. Tex.); Turrentine v. Blackwood, 4 A. B. R. 338, 28 So. 95 (Sup. Ct. Ala.); In re Emslie, 4 A. B. R. 126, 102 Fed. 291 (C. C. A.); In re Reynolds, 11 A. B. R. 758, 127 Fed. 760 (D. C. Mont.); In re Brooks, 1 A. B. R. 531, 91 Fed. 508 (D. C. Vt.); inferentially, In re Granite City Bank, 14 A. B. R. 404, 137 Fed. 818 (C. C. A. Iowa); In re Pittelkow, 1 A. B. R. 473,

92 Fed. 901 (D. C. Wis.); Keegan v. King, 3 A. B. R. 79, 96 Fed. 758 (D. C. Ind.); In re Antigo Screen & Door Co., 10 A. B. R. 359, 123 Fed. 249 (C. C. A. Wis.); In re Russell & Birkett, 3 A. B. R. 658, 101 Fed. 248 (C. C. A. N. Y., distinguished in In re Spitzer, 12 A. B. R. 346, 130 Fed. 879, and in In re Kantor & Cohen, 9 A. B. R. 372); Crosby v. Spear, 11 A. B. R. 18, 613, 98 Me. 542; In re Porterfield, 15 A. B. R. 18, 138 Fed. 192 (D. C. W. Va.); In re Mertens, 12 A. B. R. 698, 131 Fed. 972 (D. C. N. Y.); inferentially, In re Lemmon & Gale Co., 7 A. B. R. 291, 112 Fed. 96 (C. C. A. Tenn.); In re Chambers Calder & Co., 3 A. B. R. 537, 98 Fed. 865 (D. C. R. I.); In re Kleinhans, 7 A. B. R. 607, 113 Fed. 107 (D. C. N. Y.); In re Lines, 13 A. B. R. 319, 133 Fed. 803 (D. C. Penn.); In re Cobb, 3 A. B. R. 130, 96 Fed. 821 (D. C. N. Car., reversed, on other grounds, in Cobb v. Overman, 6 A. B. R. 324); In re Lumber Co. (Franklin), 17 A. B. R. 446, 147 Fed. 852 (D. C. N. J.); In re Renda, 17 A. B. R. 522, 149 Fed.

LeMaster v. Spencer, 29 A. B. R. 264, 203 Fed. 210 (C. C. A. Colo.): "And the Supreme Court has repeatedly held that when under authority of the statute property is seized by receivers or the marshals and thus comes into the lawful custody of the court it has not only jurisdiction but exclusive jurisdiction to determine the question of title."

§ 1798 $\frac{1}{2}$. **Thus, Replevin Suits Not Maintainable.**—Thus, adverse claimants to property in the possession of the bankruptcy court may not resort to replevin.⁸

Murphy v. John Hofman Co., 211 U. S. 562, 21 A. B. R. 487 (quoted further at §§ 1796, 1797): "On the whole case, we are of the opinion that the seizure of these goods on a writ of replevin from another court was an unlawful invasion of the possession of the court of bankruptcy, which cannot be justified by the assertion, entirely unsupported by the evidence, that Murphy was then holding the goods, not as an officer of the court, but as an individual. For this reason the judgment is reversed and the case remanded for further proceedings not inconsistent with this opinion."

But may petition in the bankruptcy case for an order on the receiver or trustee to surrender the property claimed.⁹

§ 1799. **Thus, Landlord's Forcible Detainer Suits Not Maintainable nor Distraint.**—Proceedings to oust the bankrupt or receiver or trustee or other person in possession of the premises for the bankruptcy court, must be brought in the bankruptcy proceedings themselves, and an independent suit by the landlord will not be permitted;¹⁰ nor by the owner

614 (D. C. Penn.); *In re McMahon*, 17 A. B. R. 531, 147 Fed. 685 (C. C. A. Ohio); *O'Dell v. Boyden*, 17 A. B. R. 756, 150 Fed. 731 (C. C. A. Ohio); [1867] *In re Winter*, 1 Bank Reg. 481; [1867] *In re Vogel*, 3 B. Reg. 198 (affirming 2 B. Reg. 427); *Plaut v. Gorham Mfg. Co.*, 20 A. B. R. 269, 159 Fed. 754 (D. C. N. Y.), quoted at § 1796; *In re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa), quoted at § 1488 $\frac{1}{2}$; impliedly, *In re Empire Construction Co.*, 19 A. B. R. 704, 157 Fed. 495 (D. C. N. Y., reversed, S. C., 166 Fed. 1019, but on ground that the action sounded in tort and that it was the state court's function to determine whether it was truly so); *Bray v. United States Fidelity & Guaranty Co.*, 22 A. B. R. 363, 170 Fed. 639 (C. C. A. W. Va.), quoted at § 1813; *Graphophone Co. v. Leeds & Catlin Co.*, 23 A. B. R. 337, 174 Fed. 158 (U. S. C.), quoted post, § 1806 $\frac{1}{4}$; *In re Max Goldman*, 23 A. B. R. 497, 174 Fed. 579 (C. C. A. Ohio); *In re New England Breeders' Club*, 23 A. B. R. 689, 175 Fed. 591 (D. C. N. H.).

Contra, *Cooke v. Scovil*, 10 A. B. R. 86, 53 Atl. 692 (N. J. Sup. Ct., criticised and rejected in *Crosby v. Spear*, 11 A. B. R. 613, 98 Me. 542, as apparently ignoring the decision of

the Supreme Court in *White v. Schloerb*, 4 A. B. R. 178, 178 U. S. 542). In this case it is to be noted objection was not made to the jurisdiction until the case got into the reviewing court. Contra, instances, *In re Smith*, 9 A. B. R. 590, 121 Fed. 1014 (D. C. R. I.); *In re Freeman*, 9 A. B. R. 68 (D. C. N. Y.).

Distinct Purpose of Bankruptcy Act to Subject Administration of Estates to Control of Tribunals Having Summary Authority.—*U. S. Fidelity Co. v. Bray*, 225 U. S. 205.

8. See post, § 1875, and cases cited ante, § 1797; *White v. Schloerb*, 4 A. B. R. 178, 178 U. S. 542, quoted at § 1797; *Berman v. Smith*, 22 A. B. R. 662, 171 Fed. 735 (D. C. Ga.).

9. Instance, *Ross v. Stroh*, 21 A. B. R. 644, 165 Fed. 628 (C. C. A. La.).

10. *In re Kleinhans*, 7 A. B. R. 604, 113 Fed. 107 (D. C. N. Y.); inferentially, *In re Adams*, 14 A. B. R. 23, 134 Fed. 142 (D. C. Conn.); *In re Chambers, Calder & Co.*, 3 A. B. R. 537, 98 Fed. 865 (D. C. R. I.); *In re Duble*, 9 A. B. R. 121, 117 Fed. 794 (D. C. Penn.); *In re Schwartzman*, 21 A. B. R. 885 (D. C. S. C.); *Plaut v. Gorham Mfg. Co.*, 20 A. B. R. 269, 159 Fed. 754 (D. C. N. Y.), quoted at § 1796.

of such property to settle questions of title to fixtures.¹¹

Although, probably an independent suit for damages in personam against the trustee might be maintained, for the wrongful detention after bankruptcy and election of trustee.¹²

But in one case such independent suit, though alleged to be sounding in tort, was restrained because the landlord had waited until almost the entire estate was distributed without presenting his claim for use and occupation and was using this indirect means to get his rent.¹³ Nor will levy of distraint be permitted.¹⁴

In *re Bishop*, 18 A. B. R. 635, 153 Fed. 304 (D. C. S. Car.): "While a voluntary proceeding in bankruptcy is in effect equivalent in some respects to an assignment for the benefit of creditors, there is this essential difference—that inasmuch as the adjudication of bankruptcy is a judicial act, and thereby the property is taken in custodia legis, the landlord cannot distrain upon such property. It would be a contempt of the court for any constable or any other agent of the landlord to interfere with the possession of the court. If such a levy was attempted, the landlord would gain nothing by it."

§ 1800. Property Taken Out of Custody, etc., after Bankruptcy, Summarily Ordered Returned.—And property taken out of the custody of the bankruptcy court, or the possession of which was acquired after bankruptcy by persons not bona fide purchasers at judicial sale, may be ordered returned and even summarily ordered returned.¹⁵

11. *Keegan v. King*, 3 A. B. R. 79, 96 Fed. 758 (D. C. Ind.); *Plaut v. Gorham Mfg. Co.*, 20 A. B. R. 269, 159 Fed. 754 (D. C. N. Y.), quoted at § 1796.

12. See ante, §§ 986, 1780; also, see *In re Hunter*, 18 A. B. R. 477, 151 Fed. 904 (D. C. Pa.).

13. *In re Empire Cons. Co.*, 19 A. B. R. 704, 157 Fed. 495 (D. C. N. Y.).

14. See § 1589.

15. *In re Endl*, 3 A. B. R. 813 (D. C. Calif.); *Bryan v. Bernheimer*, 5 A. B. R. 623, 181 U. S. 188; *In re Whitener*, 5 A. B. R. 198, 105 Fed. 180 (C. C. A. Tenn.); *In re Waterloo Organ Co.*, 9 A. B. R. 427 (D. C. N. Y.); *In re Reynolds*, 11 A. B. R. 758, 127 Fed. 760 (D. C. Mont.); compare, *In re Knight*, 11 A. B. R. 1, 125 Fed. 35 (D. C. Ky.); *In re Huddleston*, 1 A. B. R. 572 (Ref. Ala.); (1867) *Samson v. Blake*, 6 B. Reg. 410, 9 Blatchf. 379; *White v. Schloerb*, 4 A. B. R. 178, 178 U. S. 542; *Metcalf v. Parker*, 9 A. B. R. 36, 187 U. S. 165; inferentially, *Hinds v. Moore*, 14 A. B. R. 1 (C. C. A. Tenn.); *obiter*, *In re Briskman*, 13 A. B. R. 59, 132 Fed. 201 (D. C. N. Y.); inferentially, *Whitney v. Wenman*, 14 A. B. R. 49, 198 U. S. 539; compare, *In re Schermerhorn*, 16 A. B. R. 509, 145 Fed. 341 (C. C. A.).

Instance, *In re Corbett*, 5 A. B. R. 224, 104 Fed. 872 (D. C. Wis.), which was the case of a bankrupt prepaying his attorney, after the filing of an involuntary petition, by designating part of his stock as payment, but where the attorney failed to remove the same until after the adjudication, the court holding that the attorney may be ordered to return the same to the custody of the bankruptcy court.

Instance, *In re Brooks*, 1 A. B. R. 531, 91 Fed. 505 (D. C. Vt.), which was where a chattel mortgagee, by a constable, locked up goods on the mortgagor's premises; thereafter the mortgagor went into bankruptcy; then the mortgagee sold out under his mortgage; held, the bankruptcy court may order the return summarily.

Instance, *replevin* by third person from sheriff holding under attachment that was nullified by the bankruptcy, where sheriff notified by referee, *In re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa), quoted at § 1488½; instance, sheriff surrendering attached property to a third party claimant, after oral notice of bankruptcy and of restraining order and receivership, *In re Lufly*, 19 A. B. R. 614, 156 Fed. 873 (D. C. N. Y.).

Babbitt, Trustee, *v. Dutcher*, 216 U. S. 102, 23 A. B. R. 519: "It was not stated in the opinion whether the assignment was prior or subsequent to the proceedings in bankruptcy. If prior thereto, then neither the court where the bankruptcy proceedings were pending nor any other court could grant a summary order disposing of the title of the adverse claimant claiming title to the policy by assignment. That could only be determined in a plenary suit, and would fall within the rule in the *Bardes and Jaquith* cases. But if the assignment was subsequent to the bankruptcy proceedings, then it would be a nullity and would be disregarded by the bankruptcy court and possession could be given to the trustee by a summary order, as in the *Bryan and Mueller* cases."

And, it would seem under the doctrine of *Acme Harvester Co. v. Beekman* that property transferred by or taken out of the hands of the bankrupt after the filing of the bankruptcy would be property thus taken out of the custody of the bankruptcy court equally as much as if taken out of the possession of a marshal or receiver.¹⁶

Thus, subsequent to adjudication, the concealment or the removal by a bankrupt, in collusion with another, of property which was in the bankrupt's possession at the time of adjudication, is an interference with the custody of the bankruptcy court and summary jurisdiction exists over the parties thereto.

Clay v. Waters, 24 A. B. R. 298, 178 Fed. 385 (C. C. A. Mo.): "But the property here in controversy was in the possession of the bankrupt when the petition was filed and when the adjudication was made and it then passed within the jurisdiction of the District Court below. The District Court sitting in bankruptcy has jurisdiction to determine by summary proceedings, after a reasonable notice to claimants to present their claims to it, controversies between the trustee and adverse claimants over liens upon and the title and possession of (1) property in the possession of the bankrupt when the petition in bankruptcy is filed, (2) property held by third parties for him, (3) property lawfully seized by the marshal as the bankrupt's under clause 3 of section 2 of the Bankruptcy Law, and (4) property claimed by the trustee which has been lawfully reduced to actual possession by the officers of the court." This case quoted further at § 2331½.

In *re Landis*, 18 A. B. R. 483, 151 Fed. 896 (D. C. Pa.): "I regret to differ from the learned referee, but I am constrained to do so on two grounds: The first is that the horses were in the actual custody of the District Court, acting by its receiver, and that *Cleaver's* conduct in taking them away by force was wholly without warrant. This wrongful removal might have been summarily redressed, and the order asked for by the referee might have been granted for this reason alone."

And a state court's officer, who replevies after he has orally been notified of the appointment of a receiver, is guilty of contempt.¹⁷

Thus, where, after an involuntary petition was filed but before a receiver could qualify, the bankrupt secured an order dismissing the receiver and returning the property in his hands to the bankrupt, which

16. See post, § 1807.

17. In *re Wilk*, 19 A. B. R. 178, 155 Fed. 943 (D. C. N. Y.).

forthwith made a settlement with most of its creditors and paid over to them money, but the bankruptcy petition was not dismissed, and subsequently other creditors intervened and procured adjudication of bankruptcy, it was held that the referee had summary jurisdiction to order the money returned to the trustee.

Knapp & Spencer v. Drew, 20 A. B. R. 355, 160 Fed. 413 (C. C. A.): "According to the pleadings and the proof the proceeding was one to secure a redelivery to the court of property formerly in its custody, and which it then had a right and duty to administer. The appellant in taking the money from the bankrupt after proceedings in bankruptcy had been instituted against him violated the spirit and purpose of the Bankruptcy Act by attempting to prevent the administration of the estate by the proper court after it had taken jurisdiction over it and had already taken the money in question into actual possession through its receiver. Not only so, but the officers of appellant in doing what they did, if the same was knowingly and fraudulently done, committed an offense denounced by § 29b, subd. 4, Bankruptcy Act * * * which reads: 'A person shall be punished by imprisonment for a period not to exceed two years upon conviction of the offense of having knowingly and fraudulently * * * received any material amount of property from a bankrupt after the filing of a petition, with intent to defeat this act.' Appellant clearly had no such adverse claim or right to the money as exonerated it from liability to summary proceedings for its restoration to the estate from which it had been improperly taken."

Where, however, restoration in kind has become impossible because of the commingling of property, the defendant may be ordered to pay the actual value in lieu thereof.¹⁸

§ 1801. Even Property Voluntarily Surrendered by Bankruptcy Receiver or Trustee, Still within Summary Jurisdiction.—Even property voluntarily surrendered to adverse claimants by the bankruptcy receiver without order of court, may be recovered.¹⁹

Whitney v. Wenman, 198 U. S. 539, 14 A. B. R. 51: "It is insisted that in the present case the property was voluntarily turned over by the receiver, and thereby the jurisdiction of the District Court, upon the ground herein stated, is defeated, as the property is no longer in the possession or subject to the control of the court. But the receiver had no power or authority under the allegations of this bill to turn over the property. He was appointed a temporary custodian, and it was his duty to hold possession of the property until the termination of the proceedings or the appointment of a trustee for the

¹⁸. In *re Denson*, 28 A. B. R. 158, 195 Fed. 854 (D. C. Ala.).

¹⁹. See ante, § 1657. But compare, apparently contra, *Hinds v. Moore*, 14 A. B. R. 1 (C. C. A. Tenn., reversing *In re Leeds Woolen Mills*, 12 A. B. R. 136).

But joinder of a prayer for an order on the third party to pay over the purchase price, is a waiver, and is an affirmance of the improper sale, or surrender. *Mason v. Wolkowich*, 17

A. B. R. 714, 150 Fed. 699 (C. C. A. Mass.).

Innocent holder of receiver's certificate for money borrowed, within summary jurisdiction of bankruptcy court to compel return of money paid thereon by receiver, contrary to court order. *In re Burkhalter & Co. (Rogers v. People's Bank)*, 24 A. B. R. 553, 179 Fed. 403 (D. C. Ala.), quoted at § 1780½.

bankrupt. The circumstances alleged in this bill tend to show that the transfer of this property was collusive, and certainly if the allegations be true, it was made without authority of the court. The court had possession of the property and jurisdiction to hear and determine the interests of those claiming a lien therein or ownership thereof. We do not think this jurisdiction can be ousted by a surrender of the property by the receiver, without authority of the court. Whether the rights of the claimants to the property could be litigated by summary proceedings, we need not determine."

In *re Rose Shoe Mfg. Co.*, 21 A. B. R. 725, 168 Fed. 39 (C. C. A. N. Y.): "Although the referee has found that the bank took the merchandise from the possession of the receiver without his knowledge or consent, yet if it be assumed that the receiver turned it over, still the bankruptcy court was not deprived of jurisdiction. The receiver had no authority to turn over the property."

And if the property has been sold, the proceeds may be summarily ordered surrendered.

In *re Rose Shoe Mfg. Co.*, 21 A. B. R. 725, 168 Fed. 39 (C. C. A. N. Y.): "Nor does the fact that the bank sold the shoes change the situation. The proceeds stood in their place. The court had power to direct the turning over of such proceeds to the trustee. In *Trust Nat. Bank v. Chic. Title & Trust Co.*, 14 A. B. R. 102, 198 U. S. 280, the Supreme Court said: 'The sale in the circumstances did not change the situation. The proceeds stood in the place of the property and the order returning the proceeds was equivalent to an order returning the property.'"

But where a receiver has, with the apparent assent of the bankruptcy court, vacated premises claimed by the landlord, and the landlord has made peaceable entry thereon, the trustee cannot by summary proceedings oust the landlord and retake possession.

In *re Rothschild*, 18 A. B. R. 682, 154 Fed. 194 (C. C. A. N. Y.): "The argument here has been widely extended, involving a discussion as to the general powers and limitations of courts of bankruptcy, when proceedings affecting rights of the bankrupt have been begun in a State court before the filing of the petition. It is unnecessary to enter upon any such discussion, since we are clearly of the opinion that after the representative of the bankrupt's estate (the receiver) has, with the apparent assent of the bankruptcy court, vacated premises of which a third party is claiming possession, and such third person has thereupon made peaceable entry thereon, a subsequently appointed representative of the estate (the trustee) cannot oust the third party and retake possession thereof by any such summary proceeding as this, either in a bankruptcy court or in any other court of whose procedure we have any knowledge."

No distinction seems to be made between the surrender by the receiver and by the trustee, although the trustee has title and power to alienate title.²⁰

§ 1802. Similarly, Payments or Other Transfers by Bankrupt after Filing of Bankruptcy Petition.—The possession of the bankrupt at the date of the filing of the bankruptcy petition being the possession of the bankruptcy court, payments or other transfers made by him thereafter

20. *Hebert v. Crawford*, 228 U. S. 204, 30 A. B. R. 24.

out of the assets of the bankrupt estate may be summarily recovered;²¹ thus, as to preferences.²²

§ 1803. **Whether Recovery Be Plenary or Summary.**—But it is a question whether such recovery may be by summary order or requires plenary action.²³ Some courts have held that such property cannot be summarily recovered,²⁴ and that its value may not be summarily ordered paid.²⁵

The better rule would seem to be that summary jurisdiction exists, if the right itself exists.²⁶

In *re Leigh*, 31 A. B. R. 379, 208 Fed. 486 (D. C. Ills.): "It is urged that the referee was without jurisdiction to direct the repayment, because the beam company was an adverse claimant, so that a plenary suit against it to recover the money was necessary. Since Leigh paid the execution thirteen days after the filing of the bankruptcy petition, it is clear that a summary proceeding was proper."

§ 1804. **Purchasers at Sales by Trustees or Receivers Subject to Summary Jurisdiction.**—Purchasers at judicial sales by trustees and receivers are subject to the summary jurisdiction of the bankruptcy court.²⁷

In *re Jungmann*, 26 A. B. R. 401, 186 Fed. 302 (C. C. A. N. Y.): "By voluntarily becoming a purchaser of property sold under order of the court, he submits himself to the jurisdiction of the court, and when such purchaser refuses without cause to carry out his contract he may be compelled to do so by rule or attachment issuing out of the court under whose decree the sale is had."

Mason v. Wolkowich, 17 A. B. R. 714, 150 Fed. 699 (C. C. A. Mass.): "Aside from the power of the District Court with regard to the assets of bankrupts, which is especially given it by the statutes, it has all the authority which any court exercising equitable jurisdiction has to protect its receivers and the contracts made by them. Wherever a receiver, by direction of the court appointing him, makes a sale of assets in his possession, the parties concerned in the sale are bound to recognize him as an officer of the court; and consequently the court appointing the receiver, not only has power to enforce in a summary manner the completion of the contract of sale, but the parties involved are deemed to have consented to such a proceeding."

21. Compare ante, § 543; also, see *Knapp & Spencer v. Drew*, 20 A. B. R. 355, 160 Fed. 413 (C. C. A. Neb.).

22. In *re Leigh*, 31 A. B. R. 379, 208 Fed. 486 (D. C. Ills.), quoted at § 1802.

23. *Whitney v. Wenman*, 14 A. B. R. 45, 198 U. S. 539. Compare, In *re Schermerhorn*, 16 A. B. R. 509, 145 Fed. 341 (C. C. A.). Instance, apparently plenary, but point not involved, *Plaut v. Gorham Mfg. Co.*, 20 A. B. R. 269, 159 Fed. 754 (D. C. N. Y.).

Compare, on the facts but question as to whether plenary suit necessary as against the third party to whom the trustee had delivered the assets not decided, *Hebert v. Crawford*, 228

U. S. 204, 30 A. B. R. 24, quoted at § 1807.

24. *Hinds v. Moore*, 14 A. B. R. 1 (C. C. A. Tenn., reversing In *re Leeds Woolen Mills*, 12 A. B. R. 136). Compare, In *re Rothschild*, 18 A. B. R. 682, 154 Fed. 194 (C. C. A. N. Y.).

25. *Hinds v. Moore*, 14 A. B. R. 1 (C. C. A. Tenn., reversing In *re Leeds Woolen Mills*, 12 A. B. R. 136).

26. *Knapp & Spencer Co. v. Drew*, 20 A. B. R. 355, 160 Fed. 413 (C. C. A. Iowa), quoted at § 1800.

27. But compare, incidentally, In *re Bailey*, 19 A. B. R. 470, 156 Fed. 691 (D. C. N. Y.); also, see post, § 1962.

§ 1804¹. **Holders of Receivers' Certificates.**—It has been held that holders of receivers' certificates may not sue the receiver thereon in independent plenary action but must come into the bankruptcy court and there apply for an order upon its officer in charge of the fund.²⁸

§ 1805. **Obstructive Suits Brought after Bankruptcy Court Acquires Custody.**—Obstructive suits brought after the bankruptcy court has obtained custody of the property involved, which interfere with the jurisdiction of the bankruptcy court over third parties, will be disregarded if brought in the same federal court, or be enjoined if brought in the state court.²⁹ Thus, the state court will not be permitted to restrain the trustee in bankruptcy, at the suit of the bankrupt, from carrying out a proposed compromise of a controversy with the bankrupt's wife.³⁰

§ 1806. **Thus, Foreclosure Suits, Where Bankruptcy Court Already Has Custody.**—Thus, foreclosure suits brought in the state courts, although instituted before the appointment and qualification of a trustee, are ineffectual to confer jurisdiction on the state courts where, previously, actual possession had been taken of the property by the receiver in bankruptcy.³¹

And where the bankruptcy court has actual possession, though acquired by surrender from a state court receiver, it has been held to have jurisdiction to marshal liens, etc., even on real estate, though a suit in fore-

28. Compare ante, § 1780½, and post, § 1805; also, *In re Burkhalter* (*Rogers v. People's Bank*), 24 A. B. R. 553, 179 Fed. 403 (D. C. Ala.), quoted at § 1780½.

29. *In re Kenney*, 3 A. B. R. 353, 97 Fed. 554 (D. C. N. Y., affirmed by C. C. A., 5 A. B. R. 355, 105 Fed. 897, and by Supreme Court sub nom. *Clark v. Larremore*, 9 A. B. R. 476). Inferentially, *In re Muncie Pulp Co.*, 18 A. B. R. 59, 151 Fed. 732 (C. C. A. N. Y.); *In re Schermerhorn*, 16 A. B. R. 509, 145 Fed. 341 (C. C. A.); *In re Emslie*, 4 A. B. R. 126, 102 Fed. 291 (C. C. A. N. Y.); *O'Dell v. Boyden*, 17 A. B. R. 755, 150 Fed. 731 (C. C. A. Ohio).

In re Roger Brown Co., 28 A. B. R. 336, 196 Fed. 758 (C. C. A. Iowa); *In re Swofford Bros. Dry Goods Co.*, 25 A. B. R. 282, 180 Fed. 549 (D. C. Mo.), quoted at § 1901; *In re Kimmel*, 25 A. B. R. 595, 183 Fed. 665 (D. C. Pa.); *Mitchell, etc., Co. v. Carroll*, 27 A. B. R. 894, 193 Fed. 616 (C. C. A. Ohio).

In re San Gabriel Sanatorium, 4 A. B. R. 197, 102 Fed. 310 (C. C. A. Calif.), which was a case of enjoining a foreclosure suit brought after the filing of the bankruptcy petition, where the trustee had begun suit in the Dis-

trict Court to set aside the mortgage as fraudulent.

But compare, *Crosby v. Miller*, 16 A. B. R. 805, 25 R. I. 172 (Ct. App. D. C.), wherein the lower court was reversed for dismissing a bill filed, after the election of a trustee, to declare an equitable trust upon property belonging to the bankrupt.

And compare apparently erroneous application of this principle in *Cruchet v. Red Rover Mining Co.*, 18 A. B. R. 814, 155 Fed. 486 (C. C. Mass.), quoted at § 399, the court evidently overlooking the fact that, before adjudication, the remedies of creditors are unaffected by the mere pendency of an involuntary petition. As to property not in custodia legis, see ante, § 399; also, that decisions under the law of 1867 would not be quite in point, since under that act the title of the assignee in bankruptcy reverted to the date of the filing of the petition, not as under the present act, merely to the date of the adjudication, see § 1117.

30. *In re Kranich*, 23 A. B. R. 550, 174 Fed. 908 (D. C. Pa.).

31. *In re Kellogg*, 7 A. B. R. 631, 113 Fed. 190 (D. C. N. Y., affirmed in 10 A. B. R. 7). See § 1161.

closure had been already started before the bankruptcy.³² But such could not be the rule, of course, if the receiver in the foreclosure proceedings had not surrendered possession to the bankruptcy court.³³

However, the rule properly goes no further than to prevent the ousting of the bankruptcy court from its possession of the property; for, inasmuch as the bankruptcy court has not itself jurisdiction to "foreclose" a mortgagor's equity of redemption (see post, § 1972), but may only sell free and clear of liens, obviously, where formal foreclosure is desired, the mortgagee must be permitted to maintain suit therefor in the state court, even though the property itself remain in the custody of the bankruptcy court.

In *re Victor Color & Varnish Co.*, 23 A. B. R. 177, 175 Fed. 1023 (C. C. A. N. Y.): "We are clearly of the opinion that the holder of the chattel mortgage was entitled to have his day in court, in a suit to foreclose it, and that so much of the order as refused him leave to begin such a suit, on the ground that the property was in the hands of a receiver in bankruptcy, must be reversed. It was entirely proper, however, for the bankruptcy court to refuse to give petitioner immediate possession of the property; it should remain in the custody of the receiver till the suit is determined, although, of course, if all parties agree, it may be sold and the proceeds held by the receiver. Order modified."

§ 1806¼. Attempts to Control Bankruptcy Administration by Injunctions, etc., in Other Suits.—Attempts to control the bankruptcy court in its disposition of assets, allowance of claims, etc., by injunctions or other orders in other suits will not be permitted. Thus, where the defendant in a pending patent infringement suit becomes bankrupt, the court in which the infringement suit is pending will leave all questions as to the priority of claims against the bankrupt and of the payment of moneys from its estate, to the jurisdiction of the bankruptcy court, which is exclusive; nor will the bankruptcy receiver or trustee be compelled to render any active assistance to the complainant in the infringement suit other than to produce the bankrupt's books, under subpoena.

Graphophone Co. v. Leeds and Catlin Co., 23 A. B. R. 337, 174 Fed. 158 (U. S. C. C. N. Y.): "It is not for this court to say what moneys the receiver shall or shall not pay out. All questions as to priority of claims and as to payment of moneys in the custody of the District Court should be submitted to that court for determination. If the claim be one not provable in bankruptcy presumably that court will make no provision for its payment. If it be a provable claim it is equally presumable that whatever funds there may be in the hands of receiver, over and above the expenses of administering the estate, will be retained, until all provable claims are liquidated and all questions of priority (if any arise) are determined. The whole matter is exclusively in the jurisdiction of the bankruptcy court. The receiver owes no active duty to complainant to expend the money of the estate in an effort to ascertain the facts asked for. Undoubtedly the receiver will afford all reasonable facilities, as he said he would, for the examination of the records

³². In *re Dana*, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.).

³³. See ante, § 1582.

which contain the information sought for. Personally he knows nothing about it. And the officers and employees of defendant may be produced by subpoena before the master at the same time as the books, and interrogated on the subject."

§ 1806½. **Interference Otherwise than by Suit.**—Not merely interference by suit or other legal process but other forms of interference with the custody of the bankruptcy court are equally forbidden. Thus, the mere procuring of a tax deed from the county authorities, after the bankruptcy, has been held violative of the custody of the bankruptcy court.

In *re Epstein*, 19 A. B. R. 89, 156 Fed. 42 (C. C. A. Colo.): "We do not mean that property in the course of administration under the Bankruptcy Act is exempt from taxation, or freed from tax liens or claims theretofore fastened upon it (*Swarts v. Hammer*, 194 U. S. 441, 11 Am. B. R. 708, and cases *supra*), but that it is in custodia legis, and that any act interfering with the court's possession, or with its power of control and disposal, and done without its sanction, is void. The general rule is practically conceded, but it is said that the procurement of the tax deed was not such an interference, because it merely perfected an incipient title, and did not disturb the possession. The distinction does not impress us. The issuance of the deed was the principal act connected with the sale. If effective, it extinguished the right of redemption, which was still alive, transferred to the vendee the title and right of possession, became prima facie evidence of the validity of the sale and the proceedings anterior to it, and started the statute of limitations to running against any claim to the contrary. The attempt to thus strip the court of all but the naked possession was plainly an interference with its power of control and disposal, and consequently was of no effect without its sanction, although the possession was not then disturbed."

But it is difficult to see how such a mere perfecting of legal rights could constitute interference with the court's custody. On the same principle it would seem that the mere perfecting of mechanic's liens by the filing of the affidavit after the bankruptcy would likewise constitute interference—a position not at all tenable.³⁴

§ 1807. **What Constitutes "Custodia Legis" and "Assumption of Jurisdiction."**—Actual or constructive possession by the receiver, trustee, marshal or referee, or (after the filing of the petition) by the bankrupt or his agents, constitutes "custodia legis" for the purpose of "assumption of jurisdiction" by the bankruptcy court. And the bankruptcy court "assumes jurisdiction" over property, and the property comes into "custodia legis," if it is in the custody or control of the receiver in bankruptcy, or of the trustee, marshal, referee, or (after the filing of the bankruptcy petition) of the bankrupt or his agent.³⁵

34. See ante, § 1582.

35. Instance, *Corbett v. Riddle*, 31 A. B. R. 330, 209 Fed. 811 (C. C. A. Va.); In *re McMahon*, 17 A. B. R. 532, 147 Fed. 685 (C. C. A. Ohio), a case of trustee's possession. *Abrahamson v. Bretstein*, 1 A. B. R. 44 (Ref. N. Y.); In *re Huddleston*, 1 A. B. R. 572 (Ref. Ala.); compare, In *re Schloerb*, 3 A. B. R. 224 (D. C. Wis.); In *re Kleinhans*, 7 A. B. R. 606, 113 Fed. 107, (D. C. N. Y.); In *re Duncan*, 17 A. B. R. 288, 148 Fed. 464 (D. C. S. Car.); In *re Bacon*, 20 A. B. R. 107,

Acme Harvester Co. v. Beekman Lumber Co., 222 U. S. 300, 27 A. B. R. 262: "It is none the less certain that an attachment of the bankrupt's property after the filing of the petition and before adjudication cannot operate to remove the bankrupt's estate from the jurisdiction of the bankruptcy court for the purpose of the administration under the act of Congress. It is the purpose of the bankruptcy law, passed in pursuance of the power of Congress, to establish a uniform system of bankruptcy throughout the United States, to place the property of the bankrupt under the control of the court, wherever it is found, with a view to its equal distribution among the creditors. The filing of the petition is an assertion of jurisdiction with a view to the determination of the status of the bankrupt and a settlement and distribution of his estate. The exclusive jurisdiction of the bankruptcy court is so far in rem that the estate is regarded as in custodia legis from the filing of the petition. It is true that under § 70a of the act of 1898 the trustee of the estate, on his appointment and qualification, is vested by operation of law with the title of the bankrupt as of the date he was adjudicated a bankrupt, but there are many provisions of the law which show its purpose to hold the property of the bankrupt intact from the time of the filing of the petition, in order that it may be administered under the law if an adjudication in bankruptcy shall follow the beginning of the proceedings. Paragraph 5, § 70a, in reciting the property which vests in the trustee, says there shall vest 'property which prior to the filing of the petition, the bankrupt could by any means transfer or which might have been levied upon and sold under judicial process against the bankrupt.' Under § 67c attachments within four months before the filing of the petition are dissolved by the adjudication in the event of the insolvency of the bankrupt, if its enforcements would work a preference. Provision is made for the prompt taking possession of the bankrupt's property, before adjudication if necessary (§ 69a). Every person is forbidden to receive any property after the filing of the petition, with intent to defeat the purposes of the act. These provisions, and others might be recited, show the policy and purpose of the Bankruptcy Act to hold the estate in the custody of the court for the benefit of creditors after the filing of the petition and until the question of adjudication is determined. To permit creditors to attach the bankrupt's property between the filing of the petition and the time of adjudication would be to encourage a race of diligence to defeat the purposes of the act and prevent the equal distribution of the estate among all creditors of the same class which is the policy of the law. The filing of the petition asserts the jurisdiction of the Federal court, the issuing of its

159 Fed. 424 (C. C. A. N. Y.), a case of the trustee's possession; instance receiver's possession, *Plaut v. Gorham Mfg. Co.*, 20 A. B. R. 269, 159 Fed. 754 (D. C. N. Y.), quoted at § 1796; instance, receiver's possession, *In re Landis*, 18 A. B. R. 483, 151 Fed. 896 (D. C. Pa.); instance, receiver's possession, *In re Hughes*, 22 A. B. R. 303, 170 Fed. 809 (D. C. N. J.); instance, receiver's possession, though not qualified as to bond, *Knapp & Spencer v. Drew*, 20 A. B. R. 355, 160 Fed. 413 (C. C. A. Neb.), quoted at § 1800; referee's possession [sheriff holding under nullified attachment lien at referee's

request], *In re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa); instance, bankrupt's possession, *In re Coffey*, 19 A. B. R. 148 (Ref. N. Y.); instance receiver's possession acquired by surrender from a receiver in state foreclosure suit, *In re Dana*, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.); receiver's possession, *In re Rose Shoe Mfg. Co.*, 21 A. B. R. 725, 168 Fed. 39 (C. C. A. N. Y.); *In re Schoenfield*, 27 A. B. R. 64, 190 Fed. 53 (D. C. W. Va.); contra, *In re Wells*, 8 A. B. R. 75, 114 Fed. 222 (D. C. Md.).

process brings the defendant into court, the selection of the trustee is to follow upon the adjudication, and thereupon the estate belonging to the bankrupt, held by him or for him, vests in the trustee. Pending the proceedings the law holds the property to abide the decision of the court upon the question of adjudication as effectively as if an attachment had been issued, and prevents creditors from defeating the purposes of the law by bringing separate attachment suits which would virtually amount to preferences in favor of such creditors."

Murphy v. John Hofman Co., 211 U. S. 562, 21 A. B. R. 487: "When the court of bankruptcy, through the act of its officers, such as referees, receivers or trustees, has taken possession of a res, as the property of the bankrupt, it has ancillary jurisdiction to hear and determine the adverse claims of strangers to it and its possession cannot be disturbed by the process of another court."

Clay v. Waters, 24 A. B. R. 293, 178 Fed. 385 (C. C. A. Mo.): "The District Court, sitting in bankruptcy, has jurisdiction to draw to itself and to determine by summary proceedings after reasonable notice to the claimants all controversies between the trustee and adverse claimants over liens upon and the title and possession of (1) property in the possession of the bankrupt when the petition in bankruptcy is filed, (2) property held by third parties for him, (3) property lawfully seized by the marshal as the bankrupt's under clause 3 of § 2 of the bankruptcy law, and (4) property claimed by the trustee which has been lawfully reduced to actual possession by the officers of the court."

Crosby v. Spear, 11 A. B. R. 615, 98 Me. 542: "There (in *White v. Schloerb*) the property was in the possession of the referee, here it was in the possession of the trustee. The latter was as much the officer and agent of the District Court as the former. It matters not what particular officer of the court is holding the property or what may be his title. He holds it as the agent of the court whose representative he is. His possession is its possession. It brings it within the jurisdiction of that court, and from that jurisdiction it cannot be taken by any process issuing out of this court. An adverse claimant may bring suit in the State court and try the title to the property; but after the jurisdiction of the bankruptcy court has once attached he cannot take the property in specie out of the possession of that court or of any of its agents."

Carriage Co. v. Solanas, 6 A. B. R. 227, 108 Fed. 532 (U. S. C. C. La.): "A thing is in 'custodia legis' when it is shown that it has been and is subjected to the official custody of a judicial executive officer in pursuance of his execution of a legal writ. The officer holding such a thing cannot, after he has made his return on the writ, release it on his own motion to any one claiming title to the thing. The status of the thing so seized, as to third parties, is fixed by his return, and its status can be changed only by an order of the court. If a defendant on whom a marshal is executing an attachment writ turns over movables, the ownership of which he claims, to such officer, the marshal, after he has made his return to the court showing that such things were subjected to his custody in pursuance of his execution of the court's writ, is dispossessed of any power to treat with the parties to the suit in relation to the thing being so held by him in any other than his official capacity. The thing so seized by him, without reference to the question as to whether or not the defendant turned over the property of another person, will remain, by operation of law, in custodia legis until it is withdrawn from such custody by the order of a competent court."

In re Lumber Co., 17 A. B. R. 446, 147 Fed. 852 (D. C. N. J.): "But the

judgment was against the bankrupt. The command of the writ of execution was to levy on the property of the bankrupt. This was not done. The property levied on was that of the trustee in bankruptcy. The title was in him and not in the bankrupt. Besides, he is an officer of the law. He took his title as such. The property is in custodia legis."

In *re Renda*, 17 A. B. R. 523, 149 Fed. 614 (D. C. Pa.): "The receiver is the officer of the court, and his possession is that of the court itself. The money in his hands is thus in custodia legis, against which no attachment lies."

Thus, it is broadly stated that the filing of the bankruptcy petition is itself an assumption of jurisdiction.³⁶

Acme Harvester Co. v. Beekman Co., 222 U. S. 300, 27 A. B. R. 262: "The exclusive jurisdiction of the bankruptcy court is so far in rem that the estate is regarded as in custodia legis from the filing of the petition." [Quoted further ante this section.]

In *re Jersey Island Packing Co.*, 14 A. B. R. 691, 138 Fed. 625 (C. C. A. Calif.): "The filing of a petition in bankruptcy * * * places the property of the bankrupt constructively in the custody of the court of bankruptcy."

In *re Weinger, Bergman & Co.*, 11 A. B. R. 424, 126 Fed. 875 (D. C. N. Y.): "When a petition is filed before a State court acts, the State court cannot, by any subsequent action, claim to have first taken possession of the res. The fact that the bankruptcy court may not have yet made an adjudication, and that no receiver or trustee has yet been appointed, in my opinion, is immaterial."

In *re Briskman*, 13 A. B. R. 57, 132 Fed. 201 (D. C. N. Y.): "That the property of the bankrupt comes within the jurisdiction of the bankruptcy court upon the filing of either a voluntary or an involuntary petition is not controverted."

In *re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa): "The adjudication also operated as a seizure of the property [although a sheriff was still in possession under levy made within the four months] and it was in custodia legis from that time."

But this rule is to be taken with the qualification that the property involved is not in custodia legis of the bankruptcy court unless it is in the actual or constructive possession of the marshal or receiver or (after the filing of the petition) of the bankrupt or his agent, in accordance with the principles stated; and none of the cases cited are, on their facts, contrary to this qualification.³⁷

And where, under an attachment levied before the petition was filed, the property had been put into the hands of a receiver, without notice of the petition, a sale by the state court because of the "perishable nature" of the property, will be upheld as valid.

36. Compare, post, § 1808; In *re Donnelly*, 26 A. B. R. 304, 188 Fed. 1001 (D. C. Ohio).

37. Compare, In *re Donnelly*, 26 A. B. R. 304, 188 Fed. 1001 (D. C. Ohio), wherein the court unnecessarily, it seems, reiterated the much abused phrase that the filing of the petition in

bankruptcy is a caveat and injunction, although the facts did not require the discussion, since the bankruptcy court undoubtedly has power to enjoin **even adverse claimants who are in possession** until a trustee can be elected to intervene for the protection of the rights of general creditors.

Jones v. Springer, 226 U. S. 148, 29 A. B. R. 204: "It is true that the estate is regarded as in custodia legis from the date of the petition, as against a subsequent attachment. *Acme Harvester Co. v. Beekman*, 222 U. S. 300, 27 A. B. R. 262. But in a case like the present, where, under an attachment levied before the petition was filed, the property had been put into the hands of a receiver, without notice of the petition, it is not true that all power and jurisdiction of the local court were ended before notice of the bankruptcy proceedings."

Possession, therefore, by the bankrupt, or his agent, at the time of the filing of the bankruptcy petition or afterwards is custodia legis.³⁸

The cases show considerable confusion on the above proposition (although on the facts there is very little conflict), some courts laying down the rule that possession by the bankrupt (at or after adjudication) is possession by the bankruptcy court, while other courts state the true rule as before enunciated.⁴⁰ Care, therefore, should be exercised in reading the

38. *Acme Harvester Co. v. Beekman Lumber Co.*, 222 U. S. 300, 27 A. B. R. 262; *Hebert v. Crawford*, 228 U. S. 204, 30 A. B. R. 24, quoted at § 1796; *Murphy v. Hofman Co.*, 211 U. S. 562, 21 A. B. R. 487, quoted at § 1796; *Corbett v. Riddle*, 31 A. B. R. 330, 209 Fed. 811 (C. C. A. Va.); *In re Leigh*, 31 A. B. R. 379, 208 Fed. 486 (D. C. Ills.), quoted at § 1802; *In re Denson*, 28 A. B. R. 158, 195 Fed. 854 (D. C. Ala.); inferentially, *In re Duncan*, 17 A. B. R. 268, 148 Fed. 464 (D. C. S. Car.); *In re Duble*, 9 A. B. R. 121, 117 Fed. 794 (D. C. Penn.); apparently, *Frazier v. Southern Loan & Trust Co.*, 3 A. B. R. 710, 99 Fed. 707 (C. C. A. N. C.). Contra, until adjudication, *In re Wells*, 8 A. B. R. 76, 114 Fed. 222 (D. C. Mo.); contra, until adjudication, inferentially, *In re Corbett*, 5 A. B. R. 224, 104 Fed. 872 (D. C. Wis.). But compare, *Knapp & Spencer v. Drew*, 20 A. B. R. 355, 160 Fed. 413 (C. C. A. Neb.).

40. *In re Gutman & Wenk*, 8 A. B. R. 252, 114 Fed. 1009 (D. C. N. Y.); *In re Reynolds*, 11 A. B. R. 758, 127 Fed. 760 (D. C. Mont.); *Odell v. Boyden*, 17 A. B. R. 509, 150 Fed. 731 (C. C. A. Ohio); *Mound Mines Co. v. Hawthorne*, 23 A. B. R. 242, 173 Fed. 882 (C. C. A. Colo.), quoted at § 1796.

Carter v. Hobbs, 1 A. B. R. 215, 94 Fed. 108 (D. C. Ind.): This case of *Carter v. Hobbs* is to be rejected on the other point, however, that the bankruptcy court before the Amendment of 1903 could entertain suits by trustees.

In re Beals, 8 A. B. R. 644, 116 Fed. 530 (D. C. Ind.): This case is to be rejected, however, on the point that § 67 (f) annuls legal liens on exempt property.

On the facts, *In re Briskman*, 13 A. B. R. 57, 132 Fed. 201 (D. C. N. Y.); [1867] *In re Rosenberg*, 3 B. Reg. 130.

In re Lemmon & Gale, 7 A. B. R. 291, 112 Fed. 96 (C. C. A. Tenn.), wherein the referee directed the bankrupt to hold the property until the election of a trustee.

Inferentially, *In re Emslie*, 4 A. B. R. 126, 102 Fed. 291 (C. C. A. N. Y.); inferentially, and on the facts, *Crosby v. Spear*, 11 A. B. R. 613, 98 Me. 542; inferentially, *In re Klienhaus*, 7 A. B. R. 606, 113 Fed. 107 (D. C. N. Y.): "Coincident with the filing of a petition in bankruptcy, either voluntary or involuntary, a court of bankruptcy acquires control over the estate of a bankrupt or person charged with acts of bankruptcy. It may immediately seize and lay claim to all property either in the actual possession of the bankrupt or such as may be reduced to possession. Power is conferred on the court to appoint marshals or receivers to take charge of the property of the bankrupts."

Inferentially, *Whitney v. Wenman*, 14 A. B. R. 51, 198 U. S. 539; *In re Corbett*, 5 A. B. R. 224, 104 Fed. 872 (D. C. Wis.); *In re Noel*, 14 A. B. R. 715, 137 Fed. 674 (D. C. Md.); *In re Lines*, 13 A. B. R. 318, 133 Fed. 803 (D. C. Penn.).

Inferentially, *Carpenter Bros. v. O'Connor*, 1 A. B. R. 381 (16 Ohio C. C. 526), the basis of the decision in this case really being that the bankrupt's possession was the bankruptcy court's possession and existed before the State Court's receiver was appointed.

cases on this subject to note just what the facts are in the particular case.

In *re Granite City Bk.*, 14 A. B. R. 406, 137 Fed. 818 (C. C. A. Iowa): "The chief contention of the petitioner is based upon a misconception of the scheme and policy of the Bankrupt Act. The filing of the petition in bankruptcy 'was a caveat to all the world. It was in effect an attachment and injunction. Thereafter all the property rights of the debtor were ipso facto in obedience until the final adjudication. If that were in his favor, they revived, and were again in full force. If it were against him, they were extinguished as to him, and vested in the assignee (trustee) for the purposes of the trust with which he was charged. The bankrupt became, as it were, for many purposes, *civili-ter mortuus.*' * * *

"In short, the adjudication operates as a seizure of the property of the bankrupt, by which it is taken in *custodia legis*. * * * The possession of the bankrupt without more, is transferred to the trustee. No demand for the surrender and possession of the bankrupt's property is necessary. Indeed he would stand in contempt of court were he to assert the right to hold and possess the property against the trustee. He could not maintain trespass or replevin respecting any personal property owned by him prior to the adjudication in bankruptcy."

In *re Schermerhorn*, 16 A. B. R. 509, 145 Fed. 341 (C. C. A.): "Upon the filing of a petition in bankruptcy, followed by an adjudication, all property in the possession of the bankrupt of which he claims the ownership passes at once into the custody of the court of bankruptcy, and becomes subject to its jurisdiction. * * * At the time the petition in bankruptcy was filed and at the time of the adjudication on the following day, it was the bankrupt, not the petitioner, who was in the possession of the buggies under a claim of ownership. The buggies were entered by the bankrupt in his schedules as part of his estate. They were in a building which he had rented of the petitioner, of which he had the customary keys, and over which he was exercising dominion and control as a tenant. He had within the building other property than that in controversy. All that the petitioner had in the nature of possession was a key to the back door of the building, and this he had reserved to himself without the knowledge or consent of the bankrupt, his tenant. There had been no declaration of forfeiture of the bankrupt's tenancy for nonpayment of rent or other reason, and no surrender of the possession of the building. The tenancy still subsisted. The bankrupt did not know that the petitioner claimed to have purchased the buggies, nor did he agree to hold them for him. Some time after the adjudication the petitioner gained access to the building by his rear door key, changed the locks, and then asserted exclusive adverse possession. But the buggies were then in the custody of the court, and the petitioner could gain nothing by an interference therewith. It was therefore proper for the court to repossess itself of them."

In *re Schloerb*, 3 A. B. R. 224, 97 Fed. 326 (D. C. Wis., affirmed sub nom. *White v. Schloerb*, 4 A. B. R. 178, 178 U. S. 542): "On this state of facts I am of opinion that this court obtained complete jurisdiction over the property in the possession of the bankrupts and scheduled as owned by them, from the date of adjudication on September 13th, if not from the filing of the petition, and that the property taken by the sheriff was, therefore, in *custodia legis*, and not subject to seizure on the replevin process."

In *re Duncan*, 17 A. B. R. 288, 148 Fed. 464 (D. C. S. Car.): "The filing of a petition against him is a caveat to all the world, and all persons dealing with him during the interval from that date to the date of final adjudication do

so at their peril. The property of the bankrupt, after the filing of the petition against him and before adjudication thereon, is in custodia legis. It is subject to the prehensory power of the court, and the person against whom such petition has been filed cannot make any legal disposition of it. No creditor can lay hands on it, and no court, State or federal, can attach it. It is under the sole and exclusive jurisdiction and control of the bankruptcy court, and, if such court adjudges the party a bankrupt on the petition, the title to his property vests in the trustee as of the date of the filing of the petition; that date being the point of cleavage."

Possession by the bankrupt may give jurisdiction to the bankruptcy court even if the possession is not exclusive;⁴¹ and regardless of the capacity in which he holds, whether in his own right or as agent for another.⁴²

Hebert v. Crawford, 228 U. S. 204, 30 A. B. R. 24: "The firm of Beaumont Mills claimed, however, that for value and in good faith, they had acquired the title and possession of the rice * * * thirty days before the petition in bankruptcy was filed; that they had employed Moore & Bridgeman (the bankrupts) to harvest and deliver it; and that LeBlanc who was soon thereafter elected trustee [in bankruptcy], used labor, teams and machinery of the bankrupts in harvesting and threshing the crop. The Beaumont Mills paid him, as trustee, for these services * * * [he was however a member of the firm of Beaumont Mills] * * * whatever may have been the legal or equitable rights of the Beaumont Mills under the contracts with Moore and Bridgeman [the bankrupts] and under the bill of sale of June 15, 1906, it still appears that, first, Moore & Bridgeman, and, later, LeBlanc, as trustee, engaged in gathering, threshing, hauling, and delivering the rice. This physical possession, under the decision in *Murphy v. John Hofman Co.*, 211 U. S. 562, 21 A. B. R. 487, and cases cited, gave the bankruptcy court control of the res, and authority to administer it along with all other property in their physical possession when their petition was filed. That petition operated as an attachment, and brought the rice into the custody of the bankruptcy court. * * * Nor was this jurisdiction lessened because LeBlanc, trustee, after gathering the crop, delivered the rice into the possession of Beaumont Mills at their warehouse. * * * Under these decisions the physical possession of the crop brought the property within the exclusive jurisdiction of the bankruptcy court. The finding in the summary proceeding that LeBlanc had received possession, as trustee, was conclusive against him, and was not subject to collateral attack by third persons. *Noble v. Union Pacific Logging Co.*"

Compare, *In re Mundle*, 14 A. B. R. 680, 139 Fed. 961 (D. C. N. Y.): "In view of the fact that the bankrupt was in possession of the property, and the only claim of the moving parties is, that he was so as their agent, it seems to me that it is incumbent upon them to prove their claims, and that the property in the meantime or the proceeds thereof, should remain in the possession of the representative of the court."

The possession may be constructive; thus, a "seat" or "membership" in a stock exchange is held to be in the bankrupt's possession and hence to be in custodia legis, even though the approval of a board of directors is necessary.

41. *In re Brooks*, 1 A. B. R. 531, 91 Fed. 508 (D. C. Vt.).

42. Compare, on the facts, *In re Emrich*, 4 A. B. R. 91, 101 Fed. 231 (D. C. Penn.).

O'Dell v. Boyden, 17 A. B. R. 756, 150 Fed. 731 (C. C. A. Ohio): "Did the bankrupt court have such custody of the 'membership' or 'seat' as to give it jurisdiction to bring in adverse claimants and adjudicate their rights. The New Stock Exchange is an unincorporated association having a limited membership. No formal certificate of membership is issued, and aside from repute, Henrotin's only evidence of membership consists in a letter notifying him of his election and asking him to sign the constitution and by-laws. This letter is the document referred to as the 'certificate' assigned to O'Dell. Though the membership is personal it is transferable, subject to the conditions imposed by the articles of the association already referred to. But the transfer is not made except by the acceptance of a candidate for membership who is elected in the room and stead of the retiring member. When a 'transfer' of membership is made according to the terms which clog such transfers, the transferee becomes a member and the transferor ceases to be one. It follows, therefore, that the mere execution of a paper preparatory to transferring or assigning a membership works no change in membership whatever. Thus, in 1892, this same membership which was personal to Henrotin was transferred or assigned to a partnership of which he was a member. That did not deprive Henrotin of his 'seat' or 'membership'. He continued to be a member and to exercise all of the privileges of a member. In May, 1905, he again joined one of his partners in transferring or assigning this same membership to the appellant O'Dell. Nevertheless, he continued to be and act as a member, and O'Dell did not thereby become a member. What was then the effect of these transfers or assignments made of this 'seat,' first to Holzman and Company and then to O'Dell? * * *

"The transfer and assignment preceding bankruptcy may have fastened liens upon the pecuniary results of a valid sale and transfer which may be effectually enforced in the bankruptcy court, but subject to such equitable liens as may result from such prior transfers or assignments. The 'seat' or 'membership' continued to be the 'seat' of Henrotin and was a pecuniary asset which passed to his trustee. It was as much in his custody and possession as such a species of property is capable of. To deny the trustee's possession would be to deny the capability of possession of a chose in action or other incorporeal right or equity. The possession may be constructive and not manual, but it is only so because such property is not capable of a more tangible custody. Only through a court of equity can the pecuniary value of such an asset be realized to creditors or assignees. Only by decree in personam compelling the bankrupt member, can such a transfer of membership be effectuated as will put the buyer in the place of Henrotin as a member. Over him for that purpose the bankrupt court has exclusive control, and, in this sense, also, may it be said, that the 'seat' or 'membership' was in custodia legis when the trustee sought the aid of the court to adjudicate the claims and liens asserted by O'Dell.

Thus, a receiver in a pending involuntary proceeding in New York has been held, impliedly at any rate, to have such constructive possession of timber in the State of Arkansas that a suit thereafter started in the Arkansas state court claiming the property has been enjoined.⁴³

It has also been held that the possession of a sheriff under a levy made

⁴³. In *re Muncie Pulp Co.*, 18 A. B. R. 56 (C. C. A. N. Y.): However, the case seems to be based on wrong principles as to jurisdiction. The first

court that obtained jurisdiction of the res appears to have been the Arkansas State Court.

within the four months not only is not adverse but is so much that of the bankruptcy court itself that third parties may not, after adjudication of bankruptcy, replevy from the sheriff under claim of title, where at any rate the referee has notified him to hold for the bankruptcy court and he has assented.

In *re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa): "The sheriff in an affidavit says that he was informed by the referee of the adjudication in bankruptcy and requested by him to hold the property for the referee until a trustee could be appointed, but that he continued to hold it under the writ of attachment. If he did continue to so hold it, he held it wrongfully; for the attachment was dissolved by the adjudication, and he could not thereafter rightly hold it, except for the referee or the court of bankruptcy. It is wholly immaterial whether or not he agreed with the referee to so hold it. If he remained in possession of the property, he could rightly do so only as custodian for the court of bankruptcy. It is clear, however, that he retained it at the request of the referee, and was therefore in fact the custodian of it for the time being for the court of bankruptcy, and the taking of the property from him was the taking of it directly from that court."

And similarly that third parties to whom he had surrendered possession after oral notice of the bankruptcy, and of the granting of a restraining order and of a receivership, are within the summary jurisdiction and may be required to return the property.⁴⁴

Again, it has been held that, where, during the pendency of an involuntary petition, between the entry of a decree appointing a receiver in bankruptcy and the filing of his bond, an officer of the state court takes goods of an alleged bankrupt from his possession under a writ of replevin, such seizure is an unauthorized interference with the possession of the bankruptcy court.⁴⁵

But where there had been an attempted settlement before bankruptcy, and at the time of bankruptcy, a portion of the settlement money was still undistributed in the hands of the lender's agent, who had been making the distribution, it was held the bankruptcy court had no jurisdiction over the fund except to release the trustee's claim thereto.⁴⁶

But possession by the bankrupt (at and after adjudication) is possession by the bankruptcy court.

Clay v. Waters, 24 A. B. R. 293, 178 Fed. 385 (C. C. A. Mo.): "An adjudication in bankruptcy is a seizure by the court of bankruptcy and a transfer to that court of all property in the possession of the bankrupt at the time of the adjudication in which he has any interest. Thenceforth such property is a part of

44. In *re Deeb Lufty*, 19 A. B. R. 314, 156 Fed. 873 (D. C. N. Y.).

45. In *re Alton Mfg. Co.*, 19 A. B. R. 805, 158 Fed. 367 (D. C. R. I.), quoted at § 1582. However, if the assignee in this case had had possession, the seizure would have been a seizure from the assignee rather than

from the custody of the bankruptcy court, and would have been improper, since, until adjudication, the assignee's possession was not superseded. See ante, § 1609.

46. Inferentially, not directly, In *re Smyth*, 21 A. B. R. 853, 167 Fed. 871 (D. C. Pa.).

the trust estate in the legal custody of the court for the benefit of the creditors of the bankrupt and adverse claimants."

The trustee in bankruptcy may have custody of property situated in another State.⁴⁷

And like principles apply where the property comes into the actual or constructive possession of a court in the exercise of ancillary jurisdiction.

In *re Lipman*, 29 A. B. R. 139, 201 Fed. 169 (D. C. N. J.): "The exceptant insists that she is an adverse claimant in possession, and not subject to the summary jurisdiction of the bankruptcy court. By the Bankruptcy Act, § 2, the bankruptcy courts are empowered to (cl. 3), appoint receivers to take charge of the property of bankrupts whenever absolutely necessary for its preservation; (cl. 6) bring in additional persons in the bankruptcy proceedings when necessary for the complete determination of a matter in controversy; (cl. 7) cause such estates to be collected and determine controversies in relation thereto, except as by the act otherwise provided; (cl. 15) make such orders, issue such process, and enter such judgments in addition to those specifically provided for as may be necessary for the enforcement of the provisions of this Act; and (cl. 20) exercise ancillary jurisdiction over persons or property within their respective territorial limits in aid of a receiver or trustee appointed in any bankruptcy proceedings pending in any other court of bankruptcy.

"Section 23b of the Act invoked to sustain exceptant's contention, and which limits to some extent the jurisdiction of the bankruptcy court over controversies relating to the collection, etc., of estates of bankrupts referred to in section 2, cl. 7, of the Act, relates only to suits brought by the trustees, and has no restrictive effect on the right of receivers (or trustees for that matter) to maintain or defend their possession of goods seized as those of the bankrupt. *Bryan v. Bernheimer*, 181 U. S. 188, 5 Am. B. R. 623, 21 Sup. Ct. 557, 45 L. Ed. 814; *Whitney v. Wenman*, 198 U. S. 539, 14 Am. B. R. 45, 25 Sup. Ct. 778, 49 L. Ed. 1157; *Murphy v. John Hoffman Company*, 211 U. S. 562, 21 Am. B. R. 487, 29 Sup. Ct. 154, 53 L. Ed. 327. Ancillary jurisdiction is exercised for the purpose of aiding the court of primary jurisdiction to collect the estates of bankrupts and distribute them among those entitled thereto. The following of property transferred within four months of the institution of bankruptcy proceedings in such circumstances as suggest the probability of an effort to defraud creditors, and the taking charge of it though in the possession of third parties claiming title thereto, when it may be done peaceably, or failing that, to insure by proper restraining order, its production when wanted, is necessary if the beneficent purposes of the Bankruptcy Act are to be achieved. When such property is obtained, whether willingly or reluctantly yielded, it is in the possession of the court exercising such ancillary jurisdiction, and that court, by its very possession, draws to itself the power to determine the interests therein of all parties making claim thereto, and it becomes its duty to so determine and grant complete relief, that further litigation in regard thereto may be avoided. *Fidelity Trust Co. v. Gaskill* (C. C. A., 8th Cir.), 28 Am. B. R. 4, 195 Fed. 865; *In re Rochford* (C. C. A., 8th Cir.), 10 Am. B. R. 608, 124 Fed. 182; *In re Leeds Woolen Mills* (D. C., Tenn.), 12 Am. B. R. 136, 129 Fed. 922; *In re Moody* (D. C., Iowa), 12 Am. B. R. 718, 131 Fed. 525.

⁴⁷. See ante, § 1705, et seq.; also, *Thomas v. Woods*, 23 A. B. R. 132, 173 Fed. 585 (C. C. A.), quoted at § 1706;

In re MacDougall, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.).

"Whether the goods were in the possession of the bankrupt or the petitioner at the time they were taken by the ancillary receiver, and whether they were voluntarily surrendered, or were forceably taken by the receiver (not raised by her petition), are disputed questions of fact that need not be decided. The court having undoubted jurisdiction of the subject matter of the controversy, it follows that by petitioning this court for a discovery from the receiver of his right to take such goods, and for the return thereof to her, the petitioner is estopped from challenging the court's jurisdiction over her person, even if its jurisdiction in that respect depended upon her consent or acquiescence."

§ 1808. As to Adjudication in Bankruptcy "Ipso Facto" Passing Bankrupt's Property into Custodia Legis.—It is said, somewhat broadly, that the adjudication in bankruptcy *ipso facto* passes the bankrupt's property into the custody and under the protection of the Bankruptcy court; and that from the time of the adjudication in bankruptcy, the bankrupt's property comes into the custody of the Bankruptcy Court and is in *custodia legis*.⁴⁸

In *re Reynolds*, 11 A. B. R. 760, 127 Fed. 760 (D. C. Mont.): "An adjudication of bankruptcy operates in rem, and from the moment of the adjudication the bankrupt's estate is under the jurisdiction of the bankruptcy court, which will not permit any interference with its possession, even though it be by an officer of a State court acting under its process. Being a proceeding in rem, all parties interested in the res are regarded as parties thereto, including the bankrupt and trustee, as well as the creditors, secured and unsecured. The adjudication vests in the trustee or temporary receiver the title of the bankrupt's property, and stays all seizure made within four months. An adjudication of bankruptcy has the force and effect of an attachment and an injunction. It is a caveat to all the world."

In *re Anderson*, 4 A. B. R. 640, 103 Fed. 854 (D. C. S. C., reversed, on other grounds, in 7 A. B. R. 641): "Upon an adjudication in bankruptcy, all the property of the bankrupt, of every kind and description whatsoever, falls at once in *custodia legis*. His estate belongs to the court and any withholding

48. *Keegan v. King*, 3 A. B. R. 79, 96 Fed. 758 (D. C. Ind.); In *re Granite City Bank*, 14 A. B. R. 407, 137 Fed. 818 (C. C. A. Iowa); *State Bk. v. Cox*, 16 A. B. R. 36, 143 Fed. 91 (C. C. A. Ills.); In *re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa); In *re Youngstrom*, 18 A. B. R. 572, 153 Fed. 97 (C. C. A. Colo.); In *re Hughes*, 22 A. B. R. 303, 170 Fed. 509 (D. C. N. J.). See also, § 1807, where some cases are cited wherein it is said the mere filing of the petition has such effect.

Compare, contra, or, rather, modified statement, In *re Zotti*, 26 A. B. R. 234, 186 Fed. 84 (C. C. A. N. Y., affirming S. C., 23 A. B. R. 304), quoted at § 1807.

In *re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.). This case is not contra to the author's views as expressed in the latter part of § 1270 9/10,

although the court apparently gives adhesion to the unlimited doctrine that "immediately upon and by virtue of the adjudication, all the property of the bankrupt, wherever situate and in whosoever's possession it may be, passes into the custody of the court, and upon the appointment of a trustee vests in him," the court saying: "This is undoubtedly correct and is fully sustained by the authorities cited." The proposition is not correct and never has been correct, for property does not pass "into the custody of the court" regardless of "whosoever's possession it may be in." The facts of the case and the decision of the court are wholly in conformity with the correct view, as laid down in § 1270 9/10, limiting the maxim to cases where actual custody has first been obtained.

of the property of the bankrupt by himself or others is in derogation of the rights of the trustee, who is entitled to hold it for distribution among the creditors."

But this statement is to be taken with qualifications. The adjudication does bring it within the protection of the bankruptcy court, to be sure; but this is not the same as saying that, *ipso facto*, all controversies in relation to the property, title to which by operation of law passes on adjudication to creditors, may be determined in the forum of the bankruptcy court. On adjudication, *ipso facto*, all the property becomes a proper subject for the protection of the bankruptcy court, but the forum for action is not *ipso facto* the bankruptcy court. We have heretofore [ante, § 1807] endeavored to explain the limitations upon the exercise of jurisdiction by the bankruptcy court, and to mark the boundaries of its "custodia legis," and those decisions which state the rule thus broadly are not to be considered as determining the forum for bankruptcy controversies. All the cases using the broad term mentioned will be found, on analysis, to resolve themselves into some one of the classes hereinbefore distinguished. Thus, the case *In re Reynolds*, supra, was a case of "possession by the bankrupt."

§ 1809. Real Estate Generally Considered in Bankrupt's Possession.—Real estate, unless it be actually adversely held by others,⁴⁹ generally is to be presumed, from its nature, to be within the custody of the bankrupt; therefore, unless suit already has been started, actions in relation thereto generally are to be brought in the bankruptcy court.⁵⁰

And, even if a suit in foreclosure has already been instituted, yet if the receiver for the state court voluntarily surrenders possession to the bankruptcy court, the bankruptcy court will acquire thereby complete jurisdiction to marshal liens and determine all rights to the property, even to the extent of enjoining the further prosecution of the foreclosure suit.⁵¹ How-

49. *In re Snelling*, 29 A. B. R. 818, 202 Fed. 259 (D. C. Mass.), affirmed, *Clark v. Snelling*, 30 A. B. R. 50, 205 Fed. 240 (C. C. A. Mass.).

50. Impliedly, *In re Granite City Bk.*, 14 A. B. R. 408, 137 Fed. 818 (C. C. A. Iowa); instance, *In re Noel*, 14 A. B. R. 715, 137 Fed. 694 (D. C. Md.); instance, *In re Baughman*, 15 A. B. R. 23, 138 Fed. 742 (D. C. Penn.); inferentially, *In re Donnelly*, 26 A. B. R. 304, 188 Fed. 1001 (D. C. Ohio).

Instance, *In re O'Brien*, 21 A. B. R. 14 (Ref. Mass.), though based on different grounds in the opinion. But compare, *In re Bailey*, 19 A. B. R. 470, 156 Fed. 691 (D. C. N. Y.), where a trustee in bankruptcy sold at judicial sale land which the State claimed as being land under water.

Compare case where confusion evidently arose through failure to apply the principles of § 1796, the report be-

ing absolutely barren as to who had actual or constructive possession of the real estate, the facts merely showing that the bankrupt had deeded away the property to a third person as security, taking a bond for title in return, which, in turn he had transferred to his sister, the trustee's petition being for an order upon the bankrupt to "surrender" or "turn over" the property, rather than for an order to marshal liens and sell property already in the custody of the bankruptcy court. *In re Pickens & Bro.*, 26 A. B. R. 6, 184 Fed. 954 (D. C. Ga.).

51. *In re Dana*, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.), but this case seems to base its decision on the fact that the foreclosure suit was begun within four months of the bankruptcy, a wholly immaterial consideration, since the basis of the jurisdiction was simply possession of the res.

ever, if the trustee consents that the foreclosure may occur outside the bankruptcy court, he will be bound, and cannot afterwards withdraw nor repudiate the jurisdiction in whole or in part.⁵²

§ 1810. Mere Rights of Action in Personam, Not Property "in Possession" of Bankrupt.—Mere rights of action for money judgments or decrees in personam, and for debts owing to the bankrupt, etc., where no tangible property is involved, cannot be said to constitute property in the bankrupt's possession at the time of bankruptcy, and therefore the bankruptcy does not necessarily draw litigation in relation thereto into the forum of the bankruptcy court.⁵³

§ 1811. Whether Action to Be in Bankruptcy Proceedings Themselves, or Separate Plenary Action Maintainable in United States District Court.—And such action, on reason, must be taken in the bankruptcy proceedings themselves; and a separate plenary action may not be begun in the United States District Court concerning property already in the custody of the bankruptcy court in the bankruptcy proceedings proper.⁵⁴

Nevertheless, the United States District Court in bankruptcy occasionally has entertained proceedings in the nature of plenary actions concerning property in its custody, this jurisdiction always existing and not being dependent on the Amendment of 1903.

The possession by the bankruptcy court of the res gives it jurisdiction to determine all controversies in relation thereto, but such controversies may be and occasionally have been carried on by separate proceedings, in the nature of plenary actions in the District Court itself.⁵⁵

Clay v. Waters, 24 A. B. R. 298, 178 Fed. 385 (C. C. A. Mo.): "As the District Court had jurisdiction of the \$40,000 which was in the possession of the bankrupt at the time of the adjudication with a part of which the defendant purchased the real estate and obtained the promissory notes and mortgages which were the subject matter of the plenary suit against him, and as that court had ample power to determine the controversies between the trustee and the defendant concerning all this property by summary proceedings upon reasonable

⁵². *Furth v. Stahl*, 10 A. B. R. 442, 205 Penn. 439.

⁵³. Yet compare. *In re Emslie*, 4 A. B. R. 126, 102 Fed. 291 (C. C. A. N. Y.), where the bankruptcy court stayed a suit to foreclose a subcontractor's lien which had been commenced after the bankruptcy, the bankrupt being the head contractor, although obviously the only property involved was the mere right in action of the bankrupt for a money judgment, to recover a debt from the owner.

⁵⁴. *In re Noel*, 14 A. B. R. 719, 137 Fed. 694 (D. C. Md.); *Real Estate Trust Co. v. Thompson*, 7 A. B. R. 520, 112 Fed. 945 (D. C. Penn.); *In re McMahon*, 17 A. B. R. 532, 147 Fed. 685 (C. C. A. Ohio); compare, contra in-

stance, *Carriage Co. v. Solanas*, 6 A. B. R. 221, 108 Fed. 532 (D. C. La.); *Chattanooga Nat'l Bk. v. Rome Iron Co.*, 3 A. B. R. 582 (D. C. Ga.). But compare, apparently contra, *Ryttenberg v. Schefer*, 11 A. B. R. 658, 131 Fed. 313 (D. C. N. Y.).

But compare, apparently contra practice, *In re Mundle*, 14 A. B. R. 680, 139 Fed. 691 (D. C. N. Y.), in which case, however, perhaps, the court did not mean that an independent action should be instituted, but only that a hearing upon original testimony and not affidavits was proper.

⁵⁵. Instance, *Clemishaw v. Int. Shirt & Collar Co.*, 21 A. B. R. 616, 165 Fed. 797 (D. C. N. Y.).

notice to him, it also had jurisdiction of a plenary suit to determine them. The defendant may not successfully object that the District Court was powerless in such a suit because it thereby gave to him a longer notice and a better opportunity to prepare and present his claim to the property than the common practice in bankruptcy approved."

Or by summary proceedings in the referee's court, in either event the proceedings being in the District Court and in the bankruptcy court and properly entitled in the bankruptcy case. Possession of the res confers jurisdiction whether it be before the District Judge or before the referee, and it is not dependent on the Amendment of 1903. The right to begin plenary actions in the federal courts, conferred by the Amendment of 1903, relates merely to property not in the possession of the bankruptcy court, but sought to be recovered from adverse claimants.⁵⁶ Likewise, the right to prosecute suits in the federal courts by the defendants' consent, conferred by the original Act itself in § 23, refers only to cases where either property is sought to be recovered or a judgment in personam obtained against a third party.⁵⁷ But such plenary jurisdiction over adverse claimants in possession is different from the jurisdiction here being considered, which is dependent wholly on the possession of the res and which is exercisable either by the referee or by the District Judge by proceedings which, in their nature, are neither strictly summary nor yet fully plenary. So that, unless relegated to the summary proceedings before the referee by general reference to the referee or otherwise, the trustee may institute, and occasionally has instituted, proceedings to marshal liens directly in the District Court; and adverse claimants likewise may resort there although such practice is not to be favored so long as the res is already in the custody of the referee. These actions perhaps, strictly speaking, are neither "plenary" nor "summary." They do not follow any of the established forms of plenary actions, yet they are on due notice and hearing, subject to appeal or review and on that account are not perhaps, to be termed, strictly, "summary," either.⁵⁸

Thus, a mortgagee who alleged that he had been induced to release his mortgage lien by the false and fraudulent statements of the officers of the bankrupt corporation, has been permitted to institute a plenary action in the District Court, wherein the bankruptcy proceedings were pending, for the purpose of effecting a re-establishment of his lien.⁵⁹

Adverse claimants likewise may resort to the District Court although such practice is not to be favored so long as the res is already in the custody of the referee.⁶⁰

56. In re McMahon, 17 A. B. R. 531, 147 Fed. 685 (C. C. A. Ohio). Compare, Carriage Co. v. Solanas, 6 A. B. R. 221, 108 Fed. 532 (D. C. La.).

57. Compare, In re Stæuer, 5 A. B. R. 209, 104 Fed. 976 (D. C. Mass.), in which case a bond had been given to answer for the property.

58. In re Noel, 14 A. B. R. 719, 137 Fed. 694 (D. C. Md.); In re McMahon,

17 A. B. R. 531, 147 Fed. 685 (C. C. A. Ohio); Whitney v. Wenman, 14 A. B. R. 45, 198 U. S. 539.

59. Cleminshaw v. Int. Shirt & Collar Co., 21 A. B. R. 616, 165 Fed. 797 (D. C. N. Y.).

60. Instance, Cleminshaw v. Int. Shirt & Collar Co., 21 A. B. R. 616, 165 Fed. 797 (D. C. N. Y.).

§ 1812. **Nor in State Court, nor in United States District Court.**—Nor, on reason, may a separate plenary action be begun in the state court or in a federal⁶¹ court other than the bankruptcy court, while the property is in the custody of the bankruptcy court.⁶²

§ 1813. **Bankruptcy Court Permitting Controversies over Property in Its Possession to Be Carried on Elsewhere.**—But it has been held that the bankruptcy court may permit controversies over property in its possession to be carried on elsewhere, and to this end may authorize suits in state courts to be instituted or maintained by or against trustees; thus, as to suits concerning mechanics' liens;⁶³ also as to mortgages, for their foreclosure.⁶⁴

Obiter, *In re Zehner*, 27 A. B. R. 536, 193 Fed. 787 (D. C. La.): "Whether the trustee abandons the mortgaged property voluntarily or is forced to do so by order of court, this court can certainly grant permission to the mortgage creditor to foreclose in the state court. * * * But it seems to me, however, that in all cases where it is probable a surplus will be realized over and above the liens, it would be better for all parties concerned that the property be sold through the bankruptcy court."

Likewise, it has been held, that the bankruptcy court may permit its own trustee to be sued in the state court in a suit started by a chattel mortgagee after the bankruptcy, in order to determine the validity of his chattel mortgage, but will retain custody of the property involved, or sell it and retain its proceeds, to await the outcome of the decision; and that the state court has jurisdiction unless enjoined.⁶⁵

Likewise, the bankruptcy court has refused to hear summarily the question of title to lands claimed by the state to belong to the public as being land under water and has required plenary action to be instituted therefor.⁶⁶ Again, it has been held that under order of the bankruptcy court, property in controversy may be deposited with a third party, or may be sold and its proceeds be thus deposited, to await the outcome of an independent

61. *Bray v. U. S. Fidelity & Guaranty Co.*, 22 A. B. R. 363, 170 Fed. 639 (C. C. A. W. Va.).

62. See inferentially, cases cited ante, § 1797—"After the Bankruptcy Court Has Once Assumed Jurisdiction, etc."

In re McMahon, 17 A. B. R. 532, 147 Fed. 685 (C. C. A. Ohio); *Odell v. Boyden*, 17 A. B. R. 755, 150 Fed. 731 (C. C. A. Ohio); *In re Muncie Pulp Co.*, 18 A. B. R. 56, 151 Fed. 732 (C. C. A. N. Y.).

Contra, *Crosby v. Miller*, 16 A. B. R. 805, 25 R. I. 172 (Ct. App. D. C.), wherein the lower court was reversed for dismissing a bill in equity of a third party to declare a trust upon property evidently in the custody of the bank-

ruptcy court and title to which was in the bankrupt.

63. *In re Grissler*, 13 A. B. R. 508, 136 Fed. 754 (C. C. A. N. Y.).

64. *In re Victor Color & Varnish Co.*, 23 A. B. R. 177, 175 Fed. 1023 (C. C. A. N. Y.), quoted ante, § 1806.

Compare, where permission refused, *In re Zehner*, 27 A. B. R. 536, 193 Fed. 787 (D. C. La.).

65. *In re Johnson*, 11 A. B. R. 544 (D. C. Nev.); *Skilton v. Codington*, 15 A. B. R. 810, 185 N. Y. 80; obiter, *In re Foundry & Machine Co.*, 17 A. B. R. 295, 147 Fed. 828 (D. C. Wis.). Instance, partially, *In re Nat. Lock & Metal Co.*, 19 A. B. R. 106, 155 Fed. 690 (D. C. N. Y.).

66. *In re Bailey*, 19 A. B. R. 470, 156 Fed. 691 (D. C. N. Y.).

suit to determine ownership or rights of parties therein;⁶⁷ but these cases are exceptional and do not seem to be founded on any very consistent rule. On analysis, some of them will be found to be based on a misconception or doubt as to the scope of the rule laid down by the Supreme Court in *Bardes v. Bank*, 4 A. B. R. 171, 174 U. S. 524.

And the better rule undoubtedly is that neither the state court nor the United States District [formerly, Circuit] Court has jurisdiction even by express permission of the bankruptcy court, to maintain an action the object of which is to reach and determine priorities in the distribution of the assets of a bankrupt's estate in the custody of the bankruptcy court, as the jurisdiction of the bankruptcy court is original and exclusive and it has no authority to confer jurisdiction on another court.⁶⁸

Bray v. U. S. Fidelity & Guaranty Co., 22 A. B. R. 363, 170 Fed. 639 (C. C. A. W. Va.): "If otherwise complainant had the right to assert a lien upon the property of the bankrupt contract company, such right could not be availed of by a suit in the Circuit Court, the object of which was to reach and determine priorities in the distribution of assets in the custody of the bankrupt court. Practically the effect of complainant's suit in the Circuit Court is to stay proceedings in the matter of the Evansville Contract Company, bankrupt, in the District Court, and to undertake to determine priorities or preferences in an estate in the custody and control of the latter court. This the Circuit Court is not empowered to do, for the jurisdiction of the District Courts in bankruptcy in this respect is original and exclusive. * * * Complainant's counsel insist that, as the fund sought to be subjected to the complainant's lien is within the territorial limits of the district, jurisdiction of the Circuit Court therefore attaches; but this fund which constitutes the res in this case is the estate of the bankrupt in the hands of the trustees, and in our opinion property or funds in custodia legis under the orders and decrees of a court of competent jurisdiction cannot be made the basis of jurisdiction in another court in an effort to establish liens upon such fund or property or otherwise deal with it. The District Court sitting in bankruptcy having this entire fund in custody and having complete jurisdiction to administer it, the Circuit Court has no power by its decree or order to interfere with it, nor is this want of power supplied by the order of the District Court permitting complainant's bill to be filed, for, if the Circuit Court was without jurisdiction, the District Court is not authorized to confer it."

And, of course, where the bankruptcy court relinquishes possession, or

67. *Frank v. Volkommer*, 17 A. B. R. 806, 205 U. S. 521 (affirming *Volkommer v. Frank*, 14 A. B. R. 695); *Small v. Muller*, 8 A. B. R. 448 (Sup. Ct. N. Y. App. Div.).

Apparently, instance, *In re Mundle*, 14 A. B. R. 680, 139 Fed. 691 (D. C. N. Y.), in which case, however, it does not appear whether the plenary suit was to be in the State or in the Federal Court, nor for that matter whether it were to be an independent suit or merely a hearing on original evidence in the bankruptcy proceedings themselves.

See also, *Chauncey v. Dyke Bros.*, 9 A. B. R. 444, 19 Fed. 1 (C. C. A. Ark.). Compare what appears to have been the situation in the main case, as criticised in *Carriage Co. v. Solanas*, 6 A. B. R. 221, 108 Fed. 532 (D. C. La.). Compare, similarly, *Skilton v. Codington*, 15 A. B. R. 810, 185 N. Y. 80. Compare, also, the situation in *Crosby v. Miller*, 16 A. B. R. 805, 25 R. I. 172 (Ct. App. D. C.). Compare, similarly, *In re Hudson River W. P. Co.*, 17 A. B. R. 778, 148 Fed. 877 (D. C. N. Y.).

68. But compare, §§ 1584, 1584½.

declines to take actual possession, or has only constructive possession, it may permit controversies over it to be litigated in independent suits in state courts. Thus, it has been held that the bankruptcy court may, in its discretion, refuse to enjoin the prosecution of a foreclosure suit although instituted after the mortgagor's adjudication, and may simply order the trustee to intervene in the state court.⁶⁹ Again, a trustee consenting to the sale of real estate under foreclosure of mortgage in the State Court is estopped from objecting to the jurisdiction of the state court.⁷⁰

Similarly, the bankruptcy court has surrendered possession of vessels to the admiralty court to avoid complications in the assertion of libels, but has insisted on the costs and expenses of the bankruptcy court in their preservation being a lien upon the vessels upon such surrender.⁷¹

On the other hand the bankruptcy court usually will not permit such proceedings to be carried on in the state court where a probable surplus will exist for creditors.

§ 1814. Suits in Personam against Trustees and Receivers.—But trustees and receivers in bankruptcy may be sued in the state court for trover or conversion, where no seizure of property is made in the suit.⁷²

In *re Kanter & Cohen*, 9 A. B. R. 372, 121 Fed. 984 (C. C. A. N. Y.): "If the action had been in replevin a different question would arise, but as it is we entertain no doubt that the court below properly refused the receiver's application."

69. In *re Porter*, 6 A. B. R. 259, 109 Fed. 111 (D. C. Ky.). Compare, In *re Emslie*, 4 A. B. R. 126, 102 Fed. 291, (C. C. A. N. Y.).

70. *Obiter*, *Furth v. Stahl*, 10 A. B. R. 442, 205 Penn. 439 (Penn. Sup. Ct.). See, under subject of "Conflict of Jurisdiction," § 1584.

71. In *re Hughes*, 22 A. B. R. 303, 170 Fed. 809 (D. C. N. J.).

72. See ante, § 1780. *Obiter*, In *re Russell & Birkett*, 3 A. B. R. 658, 101 Fed. 248 (C. C. A. N. Y.); In *re Spitzer*, 12 A. B. R. 346, 130 Fed. 879 (C. C. A. N. Y.); instance, *Welch v. Polley*, 11 A. B. R. 215, 177 N. Y. 117; instance, *Skilton v. Codrington*, 15 A. B. R. 810, 185 N. Y. 80. *Contra* (but as to federal court), *Treat v. Wooden*, 14 A. B. R. 736 (C. C. Mass.).

Distinction Where Property in Original Possession of Bankrupts.—It had been held that the trustee could not be sued in the State Court for conversion where the bankrupt had had apparent possession, even if he might be sued there had he gone out and attempted to take possession of property not in the bankrupt's custody, In *re Mertens*, 12 A. B. R. 709 (D. C. N. Y., reversed 16 A. B. R. 831, 147 Fed. 177): "This court cannot assent to

the doctrine that its trustee in bankruptcy is liable to an action in the State Court as for trespass, trover, or conversion, when he follows the order of the court in disposing of property in its possession. This is not a case where the receiver or trustee has taken and held and disposed of property which was outside of the possession and control and apparent ownership of the bankrupt at the time of the filing of the petition in bankruptcy, in which case this court should not and would not interfere. In such case the officer of this court would act on his own responsibility, and take his chances." To same effect, In *re Schermerhorn*, 16 A. B. R. 509, 145 Fed. 341 (C. C. A.).

Property Held Fraudulently on Secret Trust for Bankrupt's Benefit.—In one case it was held that property held fraudulently on secret trust for the bankrupt's benefit, never having been in his name or possession, could be subjected by suit in the State Court started after adjudication of bankruptcy, to the payment of a judgment creditor's claim, *Evans v. Staalle*, 11 A. B. R. 182 (Minn.). It would seem in this case that the trustee ought to have intervened: he certainly had title to the property.

In re Mertens & Co., 16 A. B. R. 831, 147 Fed. 177 (C. C. A. N. Y.): "The order under review enjoins the American Woolen Company from prosecuting an action in the Supreme Court of the State of New York which it had brought against the trustee in bankruptcy to recover the value of certain personal property alleged to belong to the woolen company, and which the trustee took into his possession as the property of the bankrupts, and sold as a part of the bankrupt's estate. The order restrains the plaintiff in an action of trover from recovering the value of the property which, if its contention is correct, never became part of the bankrupts' estate, and was converted by the trustee. In effect the order overrules several decisions of this court."

And where mortgaged property has been sold by the trustee without notice to the mortgagee, and without his consent, the mortgagee may sue the trustee for conversion.⁷³

§ 1814½. Adverse Claimants Not to Be Defeated by Bankruptcy Court Surrendering Custody.—Adverse claimants to property in the custody of the bankruptcy court are entitled to have that court pass upon their rights and may not be defeated by the bankruptcy court's relinquishment of custody.

Thus, where a trustee in bankruptcy has notice of an adverse claimant's rights to property in his custody, he is not relieved from responsibility to the adverse claimant by an order of the bankruptcy court confirming a composition and ordering the property turned back to the bankrupt, such adverse claimant not having notice.⁷⁴

In re Cadenas & Coe, 24 A. B. R. 135, 178 Fed. 158 (D. C. N. Y.): "Therefore, the trustee, being charged in general with equities upon the fund, put it out of his hands without seeking to protect those equities by reserving any part of the fund or of the consideration. If he did this without knowledge of the existence of the claim, I do not consider that the terms of the order charged him; but, if he had adequate knowledge of the claim, he was in the same position as any other person who with knowledge of existing equities attaching to a res disposes of the res—that is, he became responsible as trustee to the person injured. This correspondence leaves no doubt that the trustee had the fullest notice of the claim before the composition was confirmed and went on without advising the petitioner of the composition till he supposed it was too late. Could there be a more absolute disregard of the petitioner's rights guaranteed him specifically by this court?"

DIVISION 2.

SUMMARY JURISDICTION OVER BANKRUPTS, BANKRUPT'S AGENTS AND OTHERS NOT CLAIMING ADVERSE INTERESTS.

§ 1815. When Summary Order Will Lie on Bankrupts, and Persons Not Adverse Claimants—In General.—Property belonging to the bankrupt estate which is in the hands of the bankrupt himself or his agent,

⁷³. In re Foundry & Machine Co., 17 A. B. R. 291 (D. C. Wis.).

⁷⁴. In re Cadenas & Coe, 24 A. B. R. 135, 178 Fed. 158 (D. C. N. Y.).

or some one who lays no claim to a beneficial interest in it, the trustee may seize, if he can do so peaceably. If he cannot peaceably obtain possession he is entitled to a summary order from the bankruptcy court, in the bankruptcy proceedings themselves, requiring the party in possession to surrender the property.⁷⁵

§ 1815½. Existence Also of Plenary Jurisdiction Does Not Preclude.—The fact that the bankruptcy court also has plenary jurisdiction which might be exercised in the case does not preclude the exercise of summary jurisdiction.

In *re Holbrook Shoe & Leather Co.*, 21 A. B. R. 511, 165 Fed. 973 (D. C. Mont.): "Jurisdiction by bill in the nature of plenary suit obtains, as was held in *Whitney v. Wenman*, 198 U. S. 539; but such jurisdiction does not preclude litigation of the rights of parties in bankruptcy proceedings, as distinguished from controversies by independent suits, where the trustee applies for an order requiring one to turn over property in his possession, basing the application upon the ground that the property so held belongs to the bankrupt, and is held without color of right."

§ 1816. Outstanding Claims by Third Parties on Property in Hands of Bankrupt or Agent, Summary Jurisdiction Not Divested.

—The trustee's right summarily to seize property found in the possession of the bankrupt or his agent or in the possession of one not claiming any beneficial interest in it, or to get an order from the bankruptcy court requiring the surrender, is not affected by the fact that liens in favor of third persons exist on the property, or that third persons, not themselves in possession, are laying claim to the property; for the property is brought into the bankruptcy court subject to all liens and claims, and the rights of the lienholders and claimants will be fully protected, and can be worked out through the machinery of the bankruptcy court.⁷⁶

Thus, even where a third party had attacked the sheriff by replevin and the sheriff had given a redelivery bond and was still in custody of the property, he was held still subject to the summary order of the bankruptcy court.

In *re Francis-Valentine Co.*, 2 A. B. R. 522, 526 (C. C. A. Calif., affirming 2 A. B. R. 188): "The pendency of the action of replevin against the sheriff on behalf of the American Type Founders' Company is not ground for holding

⁷⁵. Documents and books, summary order for surrender, same as other property, instance, In *re Rosenblatt*, 16 A. B. R. 307, 143 Fed. 663 (D. C. Penn.).

Obiter, In *re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.); In *re Logan*, 28 A. B. R. 543, 196 Fed. 678 (D. C. N. Y.); obiter, In *re Rathman*, 25 A. B. R. 246, 183 Fed. 913 (C. C. A. S. D.).

⁷⁶. See cases cited under main proposition, ante, § 1794, which, of course, implies this corollary.

In *re Rochford*, 10 A. B. R. 608, 124 Fed. 182 (C. C. A. S. Dak.); In *re Wiesen Bros.*, 15 A. B. R. 27 (D. C. Penn.); obiter, In *re Jersey Island Packing Co.*, 14 A. B. R. 692, 138 Fed. 625 (C. C. A. Calif.); In *re Noel*, 14 A. B. R. 720, 137 Fed. 694 (D. C. Md.); *New River Coal Land Co. v. Ruffner*, 21 A. B. R. 474, 165 Fed. 881 (C. C. A. W. Va.), quoted at § 1610.

But, compare, though the report is so meagre as to leave facts to conjecture. In *re Pickens & Bro.*, 26 A. B. R. 6, 184 Fed. 954 (D. C. Ga.).

that the portion of the property involved in that litigation shall not be delivered to the trustee. The possession which the sheriff had of that property was not for the benefit of the American Type Founders' Company, but was antagonistic to it. The intervention of bankruptcy divested the sheriff of his possession, just as it would have divested the possession of the bankrupt itself in case a like action had been commenced against the bankrupt by the same party plaintiff. The sheriff had no right to the possession of the printing press, except upon the theory that the title was in the bankrupt. The property having been once taken from his possession upon a proper bond furnished by the American Type Founders' Company, in again securing the possession by a counter bond the sheriff asserted and relied upon the bankrupt's title. The American Type Founders' Company is not a party to the proceeding in the Bankruptcy Court, and its rights are in no way affected by the order upon the sheriff. It is not represented in the present proceedings. The question is purely one of the respective rights of the sheriff and of the trustee of the estate of the bankrupt."

This doctrine has been held even in cases where a sheriff was about to sell real estate under an execution levy made more than four months prior to bankruptcy.

In *re* Baughman, 15 A. B. R. 23, 138 Fed. 742 (D. C. Pa.): "In the present instance, while the execution creditor by virtue of its judgment has a lien upon the real estate proposed to be sold, which, antedating the bankruptcy proceedings by over four months as it does, may not be affected thereby, yet, bankruptcy having intervened, the sale and distribution of the property as well as the establishment of the correct amount due to the judgment creditor which seems to be in dispute, belongs to this court, unless it seems best to let it go on elsewhere, as might be the case if the liens were more than enough to exhaust the property leaving nothing for general creditors, although this is not always controlling and is entirely optional."

Likewise where he was about to sell personal property;⁷⁷ also where it was claimed that the bankrupt was holding the property as trustee for another.⁷⁸

§ 1817. But Beneficial Interest in Trustee Must Exist.—But a beneficial interest in the property must exist in the trustee. The bankruptcy court may not be used as a means to procure surrender from the bankrupt, of property belonging to a third party; thus, it has been held that it may not be used to procure surrender, where the vendor of the property rescinds the sale to the bankrupt and reclaims the property.⁷⁹

§ 1818. Order of Surrender before Appointment of Trustee and Even before Adjudication.—The order to turn over the property may be made even before the appointment of a trustee.⁸⁰

⁷⁷ In *re* Vastbinder, 13 A. B. R. 148, 132 Fed. 718 (D. C. Penn.).

⁷⁸ Instance (but jurisdictional questions eventually waived), *Hatch v. Curtin*, 19 A. B. R. 82, 154 Fed. 791 (C. C. A. Mass.).

⁷⁹ In *re* Eliowich, 17 A. B. R. 419 (D. C. N. Y.).

⁸⁰ In *re* Muncie Pulp Co., 14 A. B. R. 70, 151 Fed. 732 (C. C. A. N. Y.);

impliedly, In *re* Lebrecht, 14 A. B. R. 445 (D. C. Tex.); impliedly, In *re* Rosenblatt, 16 A. B. R. 306, 143 Fed. 663 (D. C. Penn.), the case of a summary order before adjudication to surrender corporate books to the receiver conducting the business. Obiter, In *re* Zotti, 26 A. B. R. 234, 186 Fed. 84 (C. C. A. N. Y.), affirming 23 A. B. R. 304, 178 Fed. 304, quoted at § 1807.

And even before adjudication such order may be made upon the bankrupt or a mere agent of the bankrupt not claiming adverse interest, where a receiver has been appointed.⁸¹

However, if the order be upon an officer holding under legal process, it may not, of course, be made before adjudication, for until then the officer is an adverse claimant and not even constructively a mere agent of the bankrupt.⁸²

§ 1819. Summary Orders on Bankrupt.—If the bankrupt refuses to turn over property in his possession or under his control, belonging to the creditors, he may be summarily ordered to do so by the bankruptcy court, upon due notice and hearing, under penalty of contempt.⁸³

In *re Purvine*, 2 A. B. R. 787, 96 Fed. 192 (C. C. A. Tex.): "It is the duty of the bankrupt to deliver to the trustee all property subject to his debts. Upon his failure to make such delivery he may be ordered by the court to do so. Unquestionably, the court has this power."

In *re Davis*, 9 A. B. R. 674 (D. C. Tex.): "That jurisdiction exists generally to require, in a summary manner, the bankrupt or a third person to pay over money or to surrender other property in his possession belonging to the

81. Impliedly, In *re Rosenblatt*, 16 A. B. R. 306, 143 Fed. 663 (D. C. Penn.); In *re Franklin*, 28 A. B. R. 278, 197 Fed. 591 (D. C. Pa.); obiter, In *re Zotti*, 26 A. B. R. 234, 186 Fed. 84 (C. C. A. N. Y., affirming 23 A. B. R. 304, 178 Fed. 304), quoted at § 1807.

82. See ante, § 1662.

83. *Mueller v. Nugent*, 7 A. B. R. 224, 184 U. S. 1; In *re DeGottardi*, 7 A. B. R. 723, 114 Fed. 328 (D. C. Calif.); In *re Deuell*, 4 A. B. R. 60, 100 Fed. 633 (D. C. Mo.); In *re Miller*, 5 A. B. R. 184, 105 Fed. 57 (D. C. Iowa); In *re Levin*, 6 A. B. R. 743 (D. C. N. Y.); In *re Goldfarb*, 12 A. B. R. 386, 131 Fed. 643 (D. C. Ga.); In *re Oliver*, 2 A. B. R. 783, 96 Fed. 85 (D. C. Calif.); In *re Schlesinger*, 4 A. B. R. 361, 102 Fed. 117 (C. C. A. N. Y., affirming 3 A. B. R. 342, 97 Fed. 920); In *re McCormick*, 3 A. B. R. 340, 99 Fed. 56 (D. C. N. Y.); In *re Mayer*, 3 A. B. R. 533, 98 Fed. 839 (D. C. Wis.); *Schweer v. Brown*, 12 A. B. R. 178, 102 Fed. 117 (C. C. A. Ark.); In *re Gerstel*, 10 A. B. R. 411, 123 Fed. 166 (D. C. Ills.); In *re Wilson*, 8 A. B. R. 612, 116 Fed. 419 (D. C. Ark.); In *re Leinweber*, 12 A. B. R. 175, 128 Fed. 641 (D. C. Conn.); In *re Anderson*, 4 A. B. R. 640 (D. C. S. C., reversed, on other grounds, *McGahan v. Anderson*, 7 A. B. R. 641, 113 Fed. 115); *Samel v. Dodd*, 16 A. B. R. 166, 142 Fed. 68 (C. C. A. Ga.); obiter, *Trust Co. v. Wallis*, 11 A. B. R. 360,

126 Fed. 464 (C. C. A. Penn.); In *re Schachter*, 9 A. B. R. 499, 109 Fed. 1010-1015 (D. C. Ga.); In *re Tudor*, 2 A. B. R. 808, 96 Fed. 942 (D. C. Colo.); In *re Tudor*, 4 A. B. R. 78, 100 Fed. 796 (D. C. Colo.); impliedly, *Boyd v. Glucklich*, 8 A. B. R. 393, 116 Fed. 131 (C. C. A. Iowa); impliedly, In *re Frankfort*, 15 A. B. R. 210 (D. C. N. Y.); impliedly, In *re Henderson*, 12 A. B. R. 351, 130 Fed. 385 (D. C. Pa.); obiter, In *re Adler*, 12 A. B. R. 19, 129 Fed. 502 (D. C. Tenn.); inferentially, In *re Lasch*, 12 A. B. R. 158 (D. C. Penn.); obiter, inferentially, In *re Felson*, 10 A. B. R. 716, 124 Fed. 288 (D. C. N. Y.); instance, In *re Weinreb*, 16 A. B. R. 702, 146 Fed. 243 (C. C. A. N. Y.); instance, In *re Friedman*, 2 A. B. R. 307 (Ref. N. Y.). Instance, bank deposit as "Manager" treated as individual, In *re Kurtz*, 11 A. B. R. 129, 125 Fed. 992 (D. C. Penn.); [1867] In *re Salkey*, 21 Fed. Cas. No. 12,253, 11 N. B. Reg. 423; [1867] In *re Dresser*, Fed. Cas. 4,077; [1867] In *re Peltasohn*, Fed. Cas. 10,912; [1867] In *re Kempner*, Fed. Cas. 7,689; [1867] In *re Speyer*, Fed. Cas. 13,239. Contra, In *re Ogles*, 2 A. B. R. 514 (Ref. Tenn.); In *re Mize*, 22 A. B. R. 577, 172 Fed. 945 (D. C. Ala.); In *re Cramer*, 23 A. B. R. 637, 175 Fed. 879 (D. C. Mass.), quoted at § 1850; obiter, In *re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.); In *re Lippman*, 25 A. B. R. 874, 184 Fed. 551 (D. C. N. Y.).

bankrupt's estate, to which no adverse title is asserted, seems to be well settled by recent adjudications; and the payment or surrender, in the one case or the other, may be required, notwithstanding the person against whom the order is directed may not consent to the jurisdiction of the court."

In *re Smith*, 3 A. B. R. 95, 100 Fed. 795 (D. C. Ga.): "It is clear to my mind that the property having been found in the possession of the bankrupt, the court is authorized to direct the trustee to take charge of it. This is, of course, not a final decision, and if Mrs. Smith can in the progress of the case demonstrate her title to the property she is permitted to do so."

Ripon Knitting Works v. Schreiber, 4 A. B. R. 299, 101 Fed. 810 (D. C. Wash., affirmed, on review, in 104 Fed. 1006): "To the merely formal objection that the bankruptcy law does not confer power upon the court to compel a bankrupt to surrender his estate to a trustee, there are two sufficient answers. In the first place, the act does give the power specifically. The seventh section requires the bankrupt to 'submit to an examination concerning the conducting of his business, the cause of his bankruptcy, his dealings with his creditors and other persons, the amount, kind and whereabouts of his property, and, in addition, all matters which may affect the administration and settlement of his estate.' Subdivision 7 of § 2 expressly confers power upon the court to 'cause the estates of bankrupts to be collected, reduced to money and distributed, and determine controversies in relation thereto;' and subdivision 13 of the same section also expressly confers power upon the court to 'enforce obedience by bankrupts, officers, and other persons to all lawful orders, by fine or imprisonment, or fine and imprisonment.'"

In *re Rosser*, 4 A. B. R. 153, 101 Fed. 562 (C. C. A. Mo., in lower court, 2 A. B. R. 746, 96 Fed. 308): "There can be no doubt that under the general rules of law and under these specific provisions of the Bankrupt Act, the court and the referee were vested with the right and subjected to the duty of making the necessary orders to require the bankrupt and all other persons who had the possession and control of the property of the bankrupt estate to surrender and deliver it to the trustee. Such orders constitute one of the essential means by which the court and the referee are empowered to collect the estate of the bankrupt. It is a broad and comprehensive power, and great caution should be exercised to observe its limits and to issue under it only lawful orders. But, without its lawful exercise, the administration of the estates of bankrupts would in many cases be so complicated and tedious that all the assets would be wasted in litigation, and the beneficent purpose of the bankrupt law would fail of accomplishment. Two essential facts limit this power and condition its lawful exercise. They are that the money or property directed to be delivered to the trustee or other officer of the court is a part of the bankrupt estate, and that the bankrupt or person ordered to deliver it has it in his possession or under his control at the time that the order of delivery is made. If the property is not a part of the estate, obviously no lawful order for its delivery to the trustee can be made. If the money or property in controversy was a part of the estate of the bankrupt, but before the order for its delivery is made he has squandered, disposed of, or lost it, so that it is not in his control or possession, and he cannot obtain and deliver it at the time the order of delivery is made, or within a reasonable time thereafter, it cannot be a lawful order, because the court may not order one to do an impossibility, and then punish him for refusal to perform it. The punishment of the bankrupt for such acts must be sought under the provisions of the bankrupt law relative to the fraudulent concealment of the property of the estate and the making of false oaths relative thereto. But, if it appears to the satisfaction of the referee or the court that property of the

bankrupt estate is in control or possession of the bankrupt, a lawful order for its delivery to the trustee may be made, and a refusal to obey this order may be punished as a contempt of court, both under the general law relative to contempts and under the specific provisions of the Bankrupt Act."

Obiter, In re Barton Bros., 18 A. B. R. 100, 149 Fed. 620 (D. C. Ark.): "Under the general rules of law, and under the specific provisions of the Bankruptcy Act, a court of bankruptcy has power and jurisdiction to make an order requiring the bankrupt to pay or deliver to his trustee in bankruptcy money or other property found to be in his possession or control, constituting a part of his estate in bankruptcy, and which he has not surrendered or accounted for, and to enforce his obedience to such order by commitment as for contempt.

"Two essential facts condition the lawful exercise of the power to require a bankrupt or other person to pay or deliver to the trustee money or property in his possession. They are that the money or property directed to be delivered to the trustee is a part of the bankrupt estate, and that the bankrupt or person ordered to deliver it has it in his possession or under his control at the time the order of delivery is made."

In re Kane, 10 A. B. R. 478, 125 Fed. 984 (D. C. Penn.): "It is not intended to punish the bankrupt for concealing assets from his trustee, for which the law otherwise provides; nor for frauds or delinquencies of which he may appear to be guilty."

In re Cotton Co., 14 A. B. R. 194, 134 Fed. 477 (D. C. Ark.): "On behalf of the respondent it is urged that, to warrant a finding against respondent, the evidence must be beyond reasonable doubt; that in view of the fact that, if an order is made requiring the respondent to pay over the money, and he fails to comply with it, he will be imprisoned for contempt of court, it is urged that the proceeding must be treated as a criminal proceeding, and be governed by the same rules. This court cannot assent to this proposition. If the fact that a failure to comply with the order of the court may result in imprisonment of the respondent for contempt makes it a criminal case, many proceedings, and especially proceedings in courts of equity, would have to be treated as criminal proceedings. The failure on the part of a defendant to execute a conveyance decreed by a court of equity in a proceeding for specific performance may be enforced by imprisonment as for contempt. Refusal to answer interrogatories in a bill of discovery, refusal to pay alimony in a divorce suit, disobedience to a writ of mandamus, or violation of injunction may result in such punishment; but no one will contend that for this reason such proceedings are in the nature of criminal actions. The punishment for contempt in bankruptcy proceedings is simply for disobedience of the judgment of the court after it is found that the respondent has money or property belonging to the bankrupt estate in his possession or under his control, and, although able to comply with the order of the court, willfully refuses to do so. These provisions in the Bankrupt Act, authorizing courts of bankruptcy to enforce obedience to their orders by punishment as for contempt are neither novel nor unusual. They were included in every Bankruptcy Act, and similar provisions have been enacted by almost every State in the Union, including the State of Arkansas. In proceedings supplemental to or in aid of execution, courts are authorized by these statutes to enforce the surrender of assets subject to execution, and for this purpose may commit to jail any person refusing to comply with such order."

In re Baum, 22 A. B. R. 295, 169 Fed. 410 (C. C. A. Ark.): "An adjudication in bankruptcy operates to transfer to the trustee the title to all of the property of the bankrupt which was subject to distribution among his creditors, and, if

it appears to the satisfaction of the court that property of the bankrupt's estate is in the control or possession of the bankrupt, a lawful order for its delivery may be made."

Partners of a bankrupt partnership are subject thereto.⁸⁴

§ 1820. No Matter in What Capacity Bankrupt Holds.—No matter in what capacity the bankrupt may be holding, if he have actual possession, custody or control, it is the bankruptcy court to which resort must be had.⁸⁵

Thus, the bankrupt cannot refuse to turn over money on the ground that it, or part of it, is the property of others from whom he has fraudulently concealed it; especially where the owners thereof, being unable to trace the money, have proved claims against the estate as general creditors.⁸⁶

Even if his possession be not exclusive, yet the jurisdiction of the bankruptcy court may not necessarily be defeated;⁸⁷ and the trustee may enter the private residence of the bankrupt, or upon his exempt homestead, to gain possession, even though it be exempt from entrance for levy of execution.⁸⁸

§ 1821. Officers of Bankrupt Corporation, Subject.—Thus, the officers of a bankrupt corporation are subject to such summary jurisdiction, as being "the bankrupt."⁸⁹

Babbitt, trustee, *v. Dutcher*, 216 U. S. 102, 23 A. B. R. 519: "Respondents, as officers of the bankrupt company, asserted no adverse claim, but denied

⁸⁴. In *re Shaffer & Stern*, 26 A. B. R. 54, 185 Fed. 549 (D. C. N. Y.), where the affairs were commingled with those of a corporation formed to take over the assets, without assuming the liabilities of the failing firm.

⁸⁵. *Hebert v. Crawford*, 228 U. S. 204, 30 A. B. R. 24, quoted at § 1807, wherein bankrupts were left in charge of their crop of rice as agents of the buyers of the rice in order to harvest it. In *re Moody*, 12 A. B. R. 718, 131 Fed. 525 (D. C. Iowa), where the bankrupt was in actual possession but was holding as "agent" for an adverse claimant.

Inferentially, In *re Mundle*, 14 A. B. R. 680, 139 Fed. 691 (D. C. N. Y.); In *re Reynolds*, 13 A. B. R. 245, 133 Fed. 584 (D. C. Mont.).

In *re Reynolds*, 11 A. B. R. 258, 127 Fed. 760 (D. C. Mont.), where the bankrupt was a chattel mortgagor in actual possession.

In *re Smith*, 3 A. B. R. 95, 100 Fed. 795 (D. C. Ga.), where the bankrupt was in actual possession as agent of wife.

In *re Bender*, 5 A. B. R. 632, 106 Fed. 573 (D. C. Ark.), in which case prop-

erty was held by the bankrupt as agent of the mortgagee and peaceably delivered over by him to the marshal.

Compare, on the facts. In *re Emrich*, 4 A. B. R. 21, 101 Fed. 231 (D. C. Penn.).

Hatch v. Curtin, 19 A. B. R. 82, 154 Fed. 791 (C. C. A. Mass.), where the bankrupt had possession of notes, etc., and proceeds of same, which were claimed to be held simply as trustee, jurisdictional questions later being waived, however.

In *re Franklin, etc., Co.*, 28 A. B. R. 278, 197 Fed. 591 (D. C. Pa.).

⁸⁶. *Cummings v. Synnot*, 25 A. B. R. 859, 184 Fed. 718 (C. C. A. Pa.).

⁸⁷. Inferentially, In *re Brooks*, 1 A. B. R. 531, 91 Fed. 508 (D. C. Vt.).

⁸⁸. *Obiter*, In *re Coffman*, 1 A. B. R. 530, 93 Fed. 432 (D. C. Tex.).

⁸⁹. In *re Alphin & Lake Cotton Co.*, 14 A. B. R. 194, 134 Fed. 477 (D. C. Ark.); In *re Famous Clothing Co.*, 24 A. B. R. 780, 179 Fed. 1015 (D. C. N. Y.); instance, In *re Meier*, 25 A. B. R. 272, 182 Fed. 799 (C. C. A. Mo.); instance, In *re Kornit Mfg. Co.*, 27 A. B. R. 244, 192 Fed. 392 (D. C. N. J.).

that the corporate records and stock books were 'documents relating to the property of the bankrupt,' and asserted that therefore the trustee in bankruptcy was not entitled to their possession. We have no doubt that the books and records in question passed, on adjudication, to the trustee, and belong in the custody of the bankruptcy court, and, there being no adverse holding, that the bankruptcy court had power upon a petition and rule to show cause to compel their delivery to the trustee."

Obiter, In re Royce Dry Goods Co., 13 A. B. R. 267, 133 Fed. 100 (D. C. Mo.): "Is it any answer in law to say that such assets is the obligation of the legal entity, the corporation, and not of the active, managing officer? The artificial being, the corporation, breathes, lives, and acts by and through its managing officers. It has no hands to hold and no pockets to conceal property. The actual custody and control of its assets are in and by its manager and director. * * * So it should follow that, for the assets intrusted to the hands of the managing officers of the bankrupt concern, they are jointly and severally liable."

Inferentially, In re Alphin & Lake Cotton Co., 12 A. B. R. 654, 131 Fed. 826 (D. C. Ark.): "Lake and Alphin, being officers of the bankrupt corporation, it was their duty, under the law, to prepare and make oath to the schedules of assets and liabilities of their corporation, as corporations can only act through their officers. In fact, for this purpose, and informing the trustee or referee as to the assets of their bankrupt concern, they are the real parties; the word 'persons,' as used in the Bankruptcy Act, including 'officers of corporations.'"

In re Muncie Pulp Co., 14 A. B. R. 73, 139 Fed. 546 (C. C. A. N. Y.): "Surely, the bankruptcy law is not so vitally defective that the court cannot direct the president of the bankrupt corporation to turn over property of the bankrupt in his hands or under his control."

Indeed, the president of a bankrupt corporation, who had been employed by it to make inventions, was held subject to a summary order of the bankruptcy court requiring him to assign to the trustee pending applications for patents thereon.⁹⁰

§ 1822. Summary Orders on Agents and Others.—Also, if the property is in the hands of a mere agent of the bankrupt, or of one holding without claim of any beneficial interest therein (other, perhaps, than for his undisputed charges as bailee), and the agent or person in possession refuses to surrender it to the trustee, the bankruptcy court may, upon due notice and hearing, summarily order the agent or person in possession to surrender it, under penalty of punishment for contempt; and a plenary suit is not necessary.⁹³

⁹⁰. In re Cantelo Mfg. Co., 26 A. B. R. 57, 185 Fed. 276 (D. C. Me.). But compare ante, § 959.

⁹³. In re Muncie Pulp Co., 14 A. B. R. 71, 139 Fed. 546 (C. C. A. N. Y.); *obiter*, Trust Co. v. Wallis, 11 A. B. R. 360, 126 Fed. 464 (C. C. A. Penn.); impliedly, In re Feldser, 14 A. B. R. 216, 134 Fed. 307 (D. C. Penn.); *obiter*, Whitney v. Wenman, 14 A. B. R. 49,

198 U. S. 539; *obiter*, In re Peacock, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.); In re Logan, 28 A. B. R. 543, 196 Fed. 678 (D. C. N. Y.); *obiter*, Johnston v. Spencer, 27 A. B. R. 800, 195 Fed. 215 (C. C. A. Colo.).

Instance, In re Davis, 9 A. B. R. 674 (D. C. Tex.), quoted ante, § 1819: Bank holding proceeds of sale, made within the four months period, of the

Mueller v. Nugent, 184 U. S. 1, 7 A. B. R. 224 (reversing *In re Nugent*, 5 A. B. R. 176, 103 Fed. 581, and affirming the lower court, 4 A. B. R. 747, 104 Fed. 530; for referee's decision, same case, see 2 N. B. N. & R. 714; distinguished and explained in *Jacquith v. Rowley*, 9 A. B. R. 529, 188 U. S. 620, and *In re Wells*, 8 A. B. R. 75, 114 Fed. 222): "The proposition was that, as matter of law, where property of the bankrupt has come into the hands of a third party before the filing of the petition in bankruptcy, as the agent of the bankrupt, and to which he asserts no adverse claim, the bankruptcy court has no power by summary proceedings to compel the surrender of the property to the trustee in bankruptcy duly appointed.

"In other words, the question reduces itself to this: Has the bankruptcy court the power to compel the bankrupt, or his agent, to deliver up money or other assets of the bankrupt, in his possession or that of some one for him, on petition and rule to show cause? Does a mere refusal by the bankrupt or his agent so to deliver up oblige the trustee to resort to a plenary suit in the Circuit Court or a State court, as the case may be?

"If it be so, the grant of jurisdiction to cause the estates of bankrupts to be collected, and to determine controversies relating thereto, would be seriously impaired, and, in many respects, rendered practically inefficient.

"The bankruptcy court would be helpless indeed if the bare refusal to turn over could conclusively operate to drive the trustee to an action to recover as for indebtedness, or a conversion, or to proceedings in chancery, at the risk of the accompaniments of delay, complication, and expense, intended to be avoided by the simpler methods of the Bankrupt Law."

Thus, as to the bankrupt's bank deposit.⁹⁴

In re Kane, 12 A. B. R. 445, 131 Fed. 386 (D. C. N. Y.): "* * * the bankruptcy court had authority and jurisdiction in a summary proceeding to compel the delivery to the trustee of money or other property belonging to the bankrupt, where it appears that such property is merely held as agent or bailee, and where it is withheld from the possession of the trustee." This was the case of an order on a bank to turn over bankrupt's deposit.

Thus, as to the wife's possession without any claim of adverse interest.⁹⁵

In re Moore, 5 A. B. R. 151, 104 Fed. 896 (D. C. W. Va.): "While title to property or moneys claimed by the trustee to belong to the bankrupt are not ordinarily to be tried by the District Court, and the claims of ownership of adverse claimants summarily be passed upon and determined by this court, yet, the ownership not being contested, the trustee should not be driven to his action to obtain possession of property of the bankrupts simply because such property is in the possession or custody of another not claiming ownership thereof. Were this the case, the trustee might be compelled to institute suit for every separate item of the bankrupt's estate not in the personal, physical possession of the bankrupt at the date of the adjudication; and the malice, caprice, or whim of the bankrupt, or the various parties who chanced to have physical control of portions of the bankrupt's estate at that date, could, on any pretext, or without pretext, nullify the entire purpose of the act."

entire stock of merchandise, as trustee to pro rate among all creditors cannot, by applying the same on its own claim after adjudication (or after the filing of the petition), become thereby an adverse claimant: it remains a mere agent.

^{94.} *In re Michaels & Lindeman*, 27 A. B. R. 299, 194 Fed. 552 (D. C. N. Y.).

^{95.} Instance, *In re Cox*, 29 A. B. R. 456, 199 Fed. 952 (D. C. N. Mex.).

Thus, as to the books and documents of a bankrupt corporation in the hands of its officer in another district.⁹⁶

Thus as to the wife's possession where her possession is colorable merely.

In *re Friedman*, 18 A. B. R. 712, 153 Fed. 939 (D. C. N. Y., affirmed in 20 A. B. R. 37, 161 Fed. 260, C. C. A.): "The story of Celia Friedman is inherently preposterous, as well as demonstrably false. I am convinced that she received (contemporaneously with the sale) \$3,850, and has since acted as the confederate of her hiding husband. Considering the relationship between Mrs. Friedman and Levinson, and the connection by marriage with Wilchick, I am convinced that the three have been acting in concert to protect the proceeds of the Friedman fraud from creditors. * * * It may be admitted that the District Court on the bankruptcy side has no power summarily to try a question of title, if any real question of title exists. It may also be admitted that the same court has no power summarily to order the appropriation by a receiver or a trustee of property obtained from the bankrupt either by fraud upon him or in pursuance of his intent to hinder, delay or defraud his creditors, if any property was so obtained. But if property which had once been in the possession of the bankrupt is found in the possession of any person, and such person is, in the opinion of the court, very clearly but a cover or receptacle for that property which as between that other person and the bankrupt is still the property of the bankrupt, or if (to vary the simile) the person who holds property which was formerly in the possession of the bankrupt is but the alter ego of the bankrupt, then a summary order is proper, and no pretended instruments of transfer, no apparatus of conveyances, should prevail."

In *re Eddleman*, 19 A. B. R. 45, 154 Fed. 160 (D. C. Ky.): "The bankrupt, however, rushed all the \$2,057.29 over to his wife, and we see no reason why she might not be regarded as his agent and stakeholder in respect to it, and it is clear that when the petition in bankruptcy was filed, and when the adjudication was made, she had in her hands of money belonging to the bankrupt the difference between \$2,057.29 and \$1,605, viz., \$452.29. It is not too much to assume that this sum was in easy reach of the husband. Certainly it was his property, and belonged to the bankrupt's estate eo instanti the adjudication. Under section 29 of the act, it might have been a somewhat serious matter to interfere with it. We shall not assume that any criminal act was committed with respect to it, but shall assume that it remains intact. Courts could not tolerate, and this court would be far from encouraging, any practices by which bankrupt debtors could convert their property into money on the eve of failure and deliver it over to wives, and then insist that the latter are adverse claimants, hoping thus to evade the powers of the bankruptcy tribunals. Under such circumstances, the wife should be regarded as agent of the husband, and treated accordingly."

Thus as to other relatives.⁹⁷ Thus, as to assignees.⁹⁸

^{96.} *Babbitt v. Dutcher*, 216 U. S. 102, 23 A. B. R. 519, quoted at § 1821.

^{97.} In *re Friedman*, 20 A. B. R. 37, 161 Fed. 260 (C. C. A. N. Y., affirming 18 A. B. R. 712).

^{98.} Compare, *Louisville Trust Co. v. Cominger*, 7 A. B. R. 421, 184 U. S.

25. In this case, however, it does not appear that the assignee still had possession. Indeed, the inference is to the contrary. See also, ante, § 1665. In *re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio), quoted at § 1665.

Obiter, In re Knickerbocker, 10 A. B. R. 383, 121 Fed. 1004 (D. C. N. Y.): "When, however, such property is merely held in the capacity of agent or bailee, the person holding it has no adverse claim thereto. * * * In such case the referee has jurisdiction by summary procedure to compel the delivery to the trustee of property belonging to the bankrupt estate, and withheld from his possession and control."

Thus, as to a "seat" or "membership" in a stock exchange, the stock exchange holding the proceeds of sale of the seat, not being an adverse holder.⁹⁹ Thus, as to compelling a treasurer to file schedules.¹

One who not only denies possession, but also makes no claim of title to property which is alleged to be in his possession, cannot consistently object to summary proceedings for the recovery of such property, on the ground that he is an "adverse claimant."²

§ 1822½. State Institution as Depositary of Funds of Bankrupt Estates.—It has been held that upon the failure of a state corporation, which has been appointed a depositary of the money of bankrupt estates, and which is in charge of the state superintendent of banking, the bankruptcy court cannot exercise summary jurisdiction to order such corporation to pay over to the officers of that court, the funds deposited with it as depositary.³

§ 1823. Corporation Agent of Bankrupt, Subject Thereto.—And it has such jurisdiction even where the agent is a corporation, the order being made upon the officer or officers of the agent corporation.⁴

In re Berkowitz, 22 A. B. R. 227, 173 Fed. 1012 (D. C. N. J.): "I regard it as a serious reflection upon the administration of the Bankruptcy Act when a merchant can organize a corporation, transfer all of his assets to the corporation, continue his business in the same manner as he had before such transfer except for a change in the name over his door, and after he has been adjudicated a bankrupt, continue to conduct his business as theretofore except for the change of the name under which he is doing business. Under such circumstances, where the bankruptcy court has before it the sworn testimony of the bankrupt as to the transaction whereby he disposed of his property to the corporation, and where that evidence shows that the transfer was null and void, it seems to me that without regard to the authorities cited above, the court could summarily take possession of the property upon the theory that the corporation is not a third party setting up an adverse claim of title, but rather is holding the property as the agent of the bankrupt." See further also, In re Berkowitz, 22 A. B. R. 231, 173 Fed. 1012.

99. Odell v. Boyden, 17 A. B. R. 755, 150 Fed. 731 (C. C. A. Ohio).

1. In re Brockton Ideal Shoe Co., 29 A. B. R. 76, 200 Fed. 745 (C. C. A. N. Y.).

2. In re Fogelman, 26 A. B. R. 742, 188 Fed. 755 (D. C. N. Y.).

3. In re Bologh, 25 A. B. R. 726, 185

Fed. 825 (D. C. N. Y.), quoted at § 1637.

4. In re Muncie Pulp Co., 14 A. B. R. 71, 139 Fed. 546 (C. C. A. N. Y.); instance, In re Kane, 12 A. B. R. 445, 131 Fed. 386 (D. C. N. Y.); In re Davis, 9 A. B. R. 670 (D. C. Tex.).

§ 1823¹. **Bankrupt's Attorney, When Subject Thereto.**—It has been impliedly held that the attorney for the bankrupt may be subject thereto,⁵ even where claiming a lien on papers of his client for services performed before the bankruptcy;⁶ but such holdings have doubtless been based, partly, at any rate, on the general doctrine that courts have summary jurisdiction over attorneys practicing at the bar, in their relations with their clients.

§ 1824. **Part Adversely Held, Part Held as Agent or Not under Claim of Beneficial Interest.**—And where part of the property is held as mere agent of the bankrupt, but the remainder is claimed by the agent as his own, summary jurisdiction exists to order the return of the property not claimed; but not of the property claimed.⁷

Likewise, the right to proceed summarily is not divested because the assignee in possession happens to be also an adverse claimant of part of the property in his individual capacity.⁸

Inferentially, *In re Thompson*, 11 A. B. R. 719, 128 Fed. 575 (C. C. A. N. Y.): In this case, however, it is to be noted that the assignee had voluntarily appeared in the first instance. The court says: "It is manifest that the court had jurisdiction to compel the assignee under the void state assignment to render an account. *Bryan v. Bernheimer*, 181 U. S. 188, 5 Am. B. R. 623, 45 L. Ed. 814. This proposition is not disputed. The petitioner, Murray, recognizing the authority of the court, appeared voluntarily before the referee, presented his account and gave testimony regarding it. Having once acquired jurisdiction of the proceeding, the court did not lose it because the investigation took a wider range than the assignee expected or intended. His present contention, carried to its logical conclusion, is that the court acquired jurisdiction of those items which he chose to admit, but not to those which he chose to dispute, and that this jurisdiction was lost the moment he asserted a claim of title in his individual capacity. If this contention were sustained an assignee for the benefit of creditors could, by the mere assertion of a colorable claim, paralyze the arm of the court of bankruptcy and defeat the

5. See post, § 2099; also see impliedly, *In re Gilroy & Bloomfield*, 14 A. B. R. 627, 140 Fed. 733 (D. C. N. Y.); *In re Martin & Co.*, 20 A. B. R. 705, 167 Fed. 236 (D. C. N. Y.), quoted at § 1423; apparently contra, but perhaps simply so on the facts, *In re Davis Tailoring Co.*, 16 A. B. R. 486, 144 Fed. 285 (D. C. N. J.).

But it has been held that where an attorney for a creditor who is subsequently employed by the bankrupt to file his bankruptcy petition and schedules, receives, on the morning of the day on which they are filed, full collection of the claim, which he immediately turns over to his client, the creditor, that the trustee must pursue the creditor, not the attorney, at least

in the absence of fraud on the attorney's part, although in the decision the court seems to concede that, if the facts were sufficient, a summary order would lie, notwithstanding the money no longer was in the attorney's possession. *In re Martin & Co.*, 20 A. B. R. 705, 167 Fed. 236 (D. C. N. Y.), quoted at § 1413, note.

6. *In re Eurich's Fort Hamilton Brewery*, 19 A. B. R. 798, 158 Fed. 644 (D. C. N. Y.). Also, see ante, § 1679.

7. *In re Lebrecht*, 14 A. B. R. 445, 135 Fed. 878 (D. C. Tex.); instance, *In re Logan*, 28 A. B. R. 543, 196 Fed. 678 (D. C. N. Y.).

8. *Obiter*, *In re Muncie Pulp Co.*, 14 A. B. R. 73, 139 Fed. 546 (C. C. A. N. Y.).

intent and purpose of the law. It is asserted by the counsel for the trustee that since the amendments of 1903, the District Court has jurisdiction of any action or proceeding which the trustee may hereafter institute if the petitioner's present contention be upheld, and that a reversal of the order, while subjecting the parties to the expense and delay of retaking the testimony, will be absolutely inconsequential for the reason that the same result must inevitably be reached in the new proceeding. Whether this contention be well founded or not we do not decide, but the possibility that it may be furnished an additional reason why a decision reached after such careful consideration should not be overthrown. The petitioner was accorded the fullest opportunity to establish his defense, every fact bearing upon the controversy is now before the court and even though the question were involved in greater doubt than it is it would seem to be the duty of the court to resolve it in favor of jurisdiction."

And the summary order should not be made upon the third person unless the goods can be followed and sufficiently identified to enable the court officer to seize them.⁹

§ 1825. Lienholder in Possession after Satisfaction of Lien.—

And a lienholder in possession after satisfaction of his lien may be ordered summarily to surrender the surplus;¹⁰ but sureties holding indemnity from the bankrupt, after exoneration of the bankrupt or satisfaction of his liability, are adverse claimants, if still asserting for themselves a lien for expenses, etc.¹¹

§ 1826. Whether Filing of Petition to Redeem from Undisputed Liens Gives Summary Jurisdiction to Order Surrender on Tender of Amount Due.—The filing of a petition to redeem property from undisputed liens perhaps gives jurisdiction summarily, upon the due notice and hearing of course, to order the surrender of the property on tender to the lienholder of the amount due, such lien perhaps not existing as an adverse beneficial interest in the property. Nevertheless, this doctrine comes dangerously near to a claim of summary jurisdiction over adverse claimants in possession, and is of doubtful authority.

Under this doctrine, however, even bailees, although lienholders by virtue of the bailment, and in actual possession at the time of the bankruptcy, have been held subject to the summary jurisdiction of the bankruptcy court, their liens following the property into the bankruptcy court.¹² And a mortgagee of real estate probably may, upon tender to him of his mort-

9. In re Jackier, 24 A. B. R. 790, 179 Fed. 720 (D. C. Pa.), quoted at § 1842.

10. In re Wiesen Bros., 15 A. B. R. 27, 138 Fed. 164 (D. C. Pa.).

Apparent instance; trustee seeking summary order against pledgee to surrender excess of collateral, court allowing, however, offset of another debt. In re Searles, 29 A. B. R. 635, 200 Fed. 893 (D. C. N. Y.).

11. In re Horgan, 21 A. B. R. 31, 164 Fed. 415 (C. C. A. Mass.).

12. In re Pratesi, 11 A. B. R. 319, 126 Fed. 588 (D. C. Del.), where the bankruptcy court on summary proceedings ordered a liveryman holding possession under his lien to surrender possession to the bankruptcy court.

gage debt, be required to execute an assignment or release of the mortgage, by summary order of the bankruptcy court.¹³

§ 1827. Custodians and Court Officers in Possession under Nullified Legal Proceedings, Not Adverse Claimants.—Custodians or court officers in possession, under void legal proceedings, as sheriffs, receivers, assignees, trustees, clerks of the court or other officers in possession of property seized under legal proceedings nullified by the bankruptcy, or in possession of the proceeds thereof, are not adverse claimants and have no beneficial interest in the property.¹⁴

Bryan v. Bernheimer, 5 A. B. R. 623, 181 U. S. 188: "The general assignment * * * did not constitute Davidson an assignee for value, but simply made him an agent of Abraham for the distribution of the proceeds of the property among Abraham's creditors. * * * The present case, involves no question of jurisdiction over a suit by a trustee against a person claiming an adverse interest in himself."

Bear v. Chase, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S. C.): "These attach-

13. In *re Bacon*, 12 A. B. R. 730, 132 Fed. 157 (D. C. N. Y.). However, this was a case of real estate which usually is in the bankrupt's possession.

14. See ante, "Conflict of Jurisdiction," § 1662. Also see ante, §§ 540, 1474 and 1661. In *re Thompson*, 11 A. B. R. 719, 128 Fed. 575 (C. C. A. N. Y., affirming 10 A. B. R. 242); *Clark v. Larremore*, 9 A. B. R. 476, 188 U. S. 486 (affirming In *re Kenney*, 5 A. B. R. 355, 105 Fed. 897 (C. C. A. N. Y.)); In *re Knickerbocker*, 10 A. B. R. 381, 121 Fed. 1004 (D. C. N. Y.).

In *re Knight*, 11 A. B. R. 1, 125 Fed. 35 (D. C. Ky.): The reasoning of this case is somewhat defective although its conclusions are correct. Had the receivership been confined merely to the custody of the property covered by the mortgage sought to be foreclosed it would not have been nullified. It was nullified because it sought to seize property by legal proceedings not covered by the lien.

In *re Lenger Wagon Co.*, 6 A. B. R. 355, 110 Fed. 927 (D. C. N. Y.). Instance, In *re Geiser*, 12 A. B. R. 208 (D. C. Mont.), in which case a constable turned back to the purchaser at execution sale the excess after satisfying a judgment for a labor claim and then denied receipt of excess.

Superseding Custody of Court Officers under Execution, Though Levy Made before the Four Months.—The same doctrine has been announced as to court officers in possession under valid execution (but not if in possession in equity where the court itself has direct custody of the res) even

where the execution levy was made prior to the four month's period and is conceded to be valid. See ante, § 1582, footnote.

In *re Vastbinder*, 13 A. B. R. 148, 132 Fed. 718 (D. C. Penn.), quoted ante, § 1582, note.

In *re Baughman*, 15 A. B. R. 23, 138 Fed. 742 (D. C. Penn.), quoted ante, at § 1582, note. But in this case the property was real estate and was presumably in the actual custody of the bankrupt, thus differentiating the case slightly from In *re Vastbinder*, where the property involved was personal property.

In *re Booth*, 2 A. B. R. 770, 96 Fed. 943 (D. C. Ga.), quoted ante, at § 1582, note. This case, however, is somewhat out of harmony with the weight of authority. Thus it appears in this case that a special judgment was obtained against the particular property of which the execution creditor already held a deed as security. In effect the execution was simply the enforcement of a lien already existing, not the obtaining of a new lien within the four months period and according to the usual rules in such cases the court first obtaining possession of the res should have been permitted to retain it.

Impliedly, In *re Zeigler Co.*, 26 A. B. R. 761, 189 Fed. 259 (D. C. Conn.); obiter, *Staunton v. Wooden*, 24 A. B. R. 736, 179 Fed. 61 (C. C. A. Cal.).

Nor is a purchaser after adjudication 24 A. B. R. 736, 179 Fed. 61 (C. C. A. from an officer holding under such a lien protected. *Staunton v. Wooden*, Calif.).

ing creditors do not occupy the relation of third persons in possession of, or adverse claimants dealing with the property of the bankrupt. * * * They are but creditors of the bankrupt, who have, in their effort to collect their money, sought an advantage which the law does not give and they cannot gain any favored position by reason of an act of theirs which the law condemns."

Leidigh Carriage Co. v. Stengel, 2 A. B. R. 383, 95 Fed. 645 (C. C. A. Ohio): "It is generally true that, as between courts of concurrent jurisdiction, the court which first obtains possession of the res must retain possession of it until the res has been finally disposed of, and any one else interested in the res must apply to that court if he desires relief with respect to the property in the possession of that court. But, as between district courts sitting in bankruptcy and State courts for the administration of insolvent estates, there is no concurrent jurisdiction. The constitution of the United States, by giving to Congress the power to pass uniform bankruptcy laws, gives to the courts in which Congress shall vest this power paramount jurisdiction in bankruptcy proceedings. The orders in bankruptcy are therefore superior to those of a State insolvency court. Section 720, which forbids a court of the United States from enjoining proceedings in a State court, expressly except bankruptcy proceedings. This is the plain intimation, by Federal and paramount law, that, where a Federal Bankruptcy Court shall take jurisdiction, there the State insolvency court must yield. Hence it is that the assignee for the benefit of creditors of the defendant company, the grantee in the deed which is by the Federal law an act of bankruptcy, may be made a party in the Bankruptcy Court, and may be required to hold the assets of the bankruptcy subject to the order of the District Court in bankruptcy."

Davis v. Bohle, 1 A. B. R. 415, 92 Fed. 325 (C. C. A. Mo., affirming, *In re Sievers*, 1 A. B. R. 117, 91 Fed. 366): "Inasmuch as an assignee under a voluntary deed of assignment is not a purchaser for value of the assigned property, but is merely an agent or trustee of the assignor and his creditors, and holds the assigned property solely for their benefit, Congress, when it provided that a general assignment should be regarded as an act of bankruptcy, did not deem it necessary to say further, and in so many words, that the assigned property might be taken from the custody of the assignee at the instance of creditors, if the assignor was subsequently adjudged a bankrupt."

In re Francis-Valentine Co., 2 A. B. R. 525, 94 Fed. 793 (C. C. A. Calif., affirming 2 A. B. R. 188): "In the present case the sheriff had possession, not in opposition to the right of the bankrupt, nor in antagonism to its title, but his possession was based entirely upon the assumption that the title was in the bankrupt. Upon the adjudication of bankruptcy the sheriff's right to the possession terminated, for the writs were dissolved, and upon the appointment of a trustee in bankruptcy the right to the immediate possession vested in the latter. There was no question of conflicting claims to be adjudicated by the District Court."

In re Kennedy, 5 A. B. R. 355, 105 Fed. 897 (C. C. A. N. Y., affirming 3 A. B. R. 353, and itself affirmed in 9 A. B. R. 476, 188 U. S. 486): "But, under the provisions of the Bankrupt Act, the judgment and the levy are to be held null and void. As a consequence, the goods have been forcibly removed, without right, from the bankrupt's possession by Clark and the sheriff, and are still to be considered a part of his estate, for the return of which the court (by explicit provision in the section) may provide summarily by order, except that the title of a bona fide purchaser for value shall not be interfered with. It makes no difference whether the creditor and sheriff, whose only title rests on 'null and void' proceedings, hold the goods themselves, or the money which represents them, nor whether, as soon as the sheriff sells under execution, it

is his duty to turn over the proceeds to the judgment creditor, nor whether under the law of New York the sheriff holds the proceeds as the agent of the creditor, nor that ordinarily such proceeds would be the property of the judgment creditor. They cannot be his property in this case, because the only proceedings through which he can make out title to retain their possession are such as the bankruptcy courts must hold to be null and void.

"A further objection to the granting of the order, based on an alleged partnership between the bankrupt and a person who put some money in the business, is sufficiently discussed in the opinion of the district judge."

In *re Chase*, 10 A. B. R. 681, 124 Fed. 753 (C. C. A. R. I.): "* * * even if assignments were strictly void as such, the assignees, until the intervention of proceedings in bankruptcy, would stand as the agents of the assignors, coupled with possession; and so, having acted innocently in their behalf, they would become entitled as such agents to receive their disbursements and a reasonable compensation, and to hold a lien therefor on the property in their hands. This was well stated by Mr. Justice Brown, then a district judge, in *Hunter v. Bing* (D. C.) 9 Fed. 277, 281, where, under a previous statute in bankruptcy, he said that the respondent in that case, who was an assignee under a common law assignment, might be regarded as a 'factor or agent' of the assignor; so that he might be held 'as having done what he did under an implied request to that effect, and to have acquired thereby an equitable lien upon the property in his possession for his necessary services and disbursements therein, which should be respected in bankruptcy so far as they have been necessary and beneficial to the general creditors, or such as the assignee in bankruptcy would otherwise have incurred.' Mr. Justice Gray, in *Bryan v. Bernheimer*, 181 U. S. 188, 192, 193, 5 Am. B. R. 623, noticed the same fact when he said that an assignee under a general assignment is not one for value, but simply 'an agent' for the distribution of the proceeds of the debtor's property among his creditors.

"Indeed, this proposition of agency is well illustrated by the fact that, ordinarily, common law assignments contain a clause expressly making the assignee the agent of the assignor; but this clause, of course, is not necessary, because, if the assignment becomes ineffectual as an assignment and as creating a technical trust, the agency is implied by law. On the other hand, it is not to be inferred that the assignor and the assignee are at liberty to create the terms of this agency at their own option. From the time the assignor declares his insolvency by making an assignment, his property must be held equitably for the benefit of his creditors, and he can do nothing which will embarrass or prejudice them in realizing therefrom, whether the result is that they are administered under the common law assignment or ultimately go into the hands of a trustee in bankruptcy. Therefore, in no event can he impress on them a lien for any amount of compensation arbitrarily agreed on. Anything in this direction beyond what would be reasonable and equitable would be contrary to the policy of the law, and would be declared invalid by the court having jurisdiction of the trust if the assignment is worked out at common law, or by the court in bankruptcy if the property finally comes under its control."

In *re Tune*, 8 A. B. R. 286, 115 Fed. 906 (D. C. Ala.): "When the only right of possession by a State court of attached property is based on an attachment lien, which is annulled by the adjudication in bankruptcy, the State court loses all jurisdiction of the rem, which is transferred into the exclusive jurisdiction of the court of bankruptcy. There is no longer any right of possession in the officer of the State court, who then holds as bailee for the per-

son rightfully entitled to possession, and becomes a trespasser if he fails to deliver on proper demand."

Indeed, it was held in one case that it was contempt of the bankruptcy court to replevy property, after bankruptcy, that was still being held by a sheriff who had seized it under an attachment within the four months period, where the sheriff had been notified by the referee.¹⁵

Indeed, court officers in possession under nullified legal liens are so far from considered as holding adversely to the bankruptcy court, that, where such officers surrender the property to a third party claimant, such third party himself is subject to summary jurisdiction and may be ordered to return the property, precisely as if taken from the custody of the bankruptcy court itself.¹⁶

In *re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio): "The assignment by Hays to Stewart did not constitute the latter an assignee for value, but simply made him the agent of Hays for the distribution of the proceeds of the property among the latter's creditors. Being such agent his possession was that of the principal and he therefore did not hold adversely to the bankrupt or to the latter's trustee by the mere fact that he held in his hands funds received by him under the assignment." Quoted further at § 1665.

§ 1828. But, until Liens Nullified, Custodians and Court Officers, "Adverse Claimants."—But, unless the legal liens are nullified, that is to say, until adjudication in bankruptcy takes place, such custodians and court officers are adverse claimants, representing creditors in possession, and may not be proceeded against summarily, although, on subsequent adjudication, they may thus be proceeded against.¹⁷

In *re Andre*, 13 A. B. R. 133 (C. C. A. N. Y.): "The attachment was process which the sheriff was bound to enforce for the benefit of the plaintiff in the action, and though it would be dissolved in the event of an adjudication of bankruptcy, it was his right and his duty to retain the property until the attachment should be dissolved, and even then until by competent authority he should be required to surrender it. Representing the party who had obtained the attachment, and as an officer whose duty it was to hold and dispose of the property in obedience to the process, he was in possession under a title paramount and adverse to that of the alleged bankrupt and he asserted his adverse title upon the application to require him to surrender the property by insisting that the application should be made to the court that had issued the process and by setting up his own lien for poundage."

Thus, a sheriff holding funds under an attachment and claiming a lien thereon for his poundage has been held an adverse claimant, not subject to summary order before adjudication.¹⁸

So, one who, long prior to the commencement of bankruptcy proceed-

15. In *re Walsh Bros.*, 20 A. B. R. 472, 159 Fed. 560, 163 Fed. 352 (D. C. Iowa), quoted at §§ 1488½, 1807.

16. In *re Deeb Luffy*, 19 A. B. R. 614, 156 Fed. 873 (D. C. N. Y.).

17. *Mather v. Coe*, 1 A. B. R. 504,

92 Fed. 333 (D. C. Ohio); *obiter*, in *Keegan v. King*, 3 A. B. R. 79, 84, 96 Fed. 758 (D. C. Ind.). See *ante*, § 1662 and § 1818.

18. In *re Andre*, 13 A. B. R. 132 (C. C. A. N. Y.).

ings, becomes the legal custodian of funds to which lien claimants are asserting rights in a state court, is an adverse claimant against whom summary proceedings for the recovery of the fund will not lie.

In *re Heintz*, 29 A. B. R. 19, 201 Fed. 338 (C. C. A. Ohio): "It is equally clear that the controversy between these parties is of such character that it can be determined only by a plenary suit in a court of competent jurisdiction. While the respondent does not claim to be the owner of the money in question, yet it holds the fund as a legal custodian for lien claimants who are asserting rights in and to it adverse to those of the trustee in bankruptcy, and who, in accordance with the law, invoked the aid of the proper State court to perfect and enforce their liens more than eighteen months prior to the filing of the petition in bankruptcy. The regularity of the proceedings to foreclose the liens is not questioned, nor can it be denied that the State court acquired complete jurisdiction and control over all the parties and property long prior to the commencement of the bankruptcy proceedings against Heintz."

But, of course, where the proceeds of an execution sale are turned over to the execution creditor, summary process will not lie, since the lien no longer exists and the creditor has become an adverse claimant in possession.¹⁹

§ 1829. Court Officers Holding under Nullified Legal Proceedings Subject to Summary Order.—But such agent or person in possession under a lien by legal proceedings which has been nullified by the adjudication of bankruptcy, even if he be a court officer, may be ordered to surrender the property to the trustee in bankruptcy, without the necessity of a plenary suit: a simple petition with notice upon the person, or upon the sheriff or other officer, upon the receiver or assignee, to show cause why he should not be ordered to surrender the property, being all that is necessary.²⁰

§ 1830. Order May Not Require Surrender of More than Is in Officer's Hands.—The order on the assignee, receiver or other court officer cannot require him to turn over more than he actually has in his possession. He cannot be required, on summary order, to make good disbursements he already has made under the assignment or levy before the bankruptcy adjudication.²¹

¹⁹ In *re Knickerbocker*, 10 A. B. R. 382, 121 Fed. 1004 (D. C. N. Y.).

Also, see cases cited under subject of "Annulment of Legal Liens," under § 67 (f), ante, § 1461.

²⁰ See, "Assignee May Be Ordered Summarily to Surrender the Assets," ante, § 1611; "Bankruptcy Court May Issue Order to Surrender the Property Involved," ante, §§ 1794, 1795.

See, in addition, *In re Cohn*, 18 A.

B. R. 786 (Ref. Calif.); *In re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio), quoted at § 1665 and at § 1827.

²¹ See ante, "No Summary Order as to Sums Already Disbursed," § 1612. Impliedly and obiter, *In re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio), quoted at § 1665 and § 1827; instance, *In re Banzai Mfg. Co.*, 25 A. B. R. 497, 183 Fed. 298 (C. C. A. N. Y.).

SUBDIVISION "A."

PROCEDURE ON SUMMARY PETITIONS.

§ 1831. Procedure on Summary Petitions, in General.—Summary jurisdiction over bankrupts and agents and others in possession not claiming adverse interest, is exercised without the usual formalities of recognized actions and without usual rule days, but, nevertheless, must be on due and reasonable notice and hearing, without impairment of constitutional rights.²²

§ 1832. What Is Summary Process.—Summary process is process, either with or without notice to the party affected, not made in accordance with the established rule days of regular suits, the court proceeding usually by order and not by judgment and execution. The process may be either by order for surrender or injunction, or by notice to appear and set up rights or be debarred.²³

Inferentially, *Doroshow v. Ott*, 14 A. B. R. 37, 134 Fed. 740 (C. C. A. N. J.): "Summary proceedings by the bankrupt court for the determination of questions of title against adverse claimants, have not ordinarily been countenanced in bankrupt legislation, and the courts have been careful to avoid giving sanction to such proceedings in a bankrupt court, as would deprive outside parties and adverse claimants of their 'day in court in the regular way—that is, by pleadings, trial and judgment.'"

Compare, *In re McMahon*, 17 A. B. R. 534, 147 Fed. 685 (C. C. A. Ohio): "The proceeding to which the petitioner McMahon was made a party was not a summary one in the strict sense of that term: It did not differ in any essential from that sustained in *Whitney v. Wenman*. Nominally an application for an order to sell property of the bankrupt in possession of the assignee, it was in its essence a petition to bring in persons asserting liens for the purpose of determining the rights of such persons, and to sell the property free from all liens. The defendants were made such by subpoena, and required to appear and answer or defend. It was in substance a plenary suit. In *Whitney v. Wenman*, the court said of the jurisdiction to determine claims to or upon the property of the bankrupt in possession of the trustee under § 2, clause 7, that it did not perceive 'that it makes any difference that the jurisdiction is not sought to be asserted in a summary proceeding, but resort is had to an action in the nature of a plenary suit, wherein the parties can be fully heard after the due course of equitable procedure.'"

Compare, impliedly, *In re Steuer*, 5 A. B. R. 213, 104 Fed. 976 (D. C. Mass.): "It remains to consider if, under the form of a petition in bankruptcy, the de-

²² *In re Frank*, 25 A. B. R. 486, 182 Fed. 794 (C. C. A. N. D.); *In re Greer*, 26 A. B. R. 811, 189 Fed. 511 (D. C. Ark.); *In re Soloway & Katz*, 28 A. B. R. 225, 196 Fed. 132 (D. C. Conn.).

²³ And compare note, *Shutts v. Bank*, 3 A. B. R. 505 (D. C. Ind.), wherein it is apparently contended that a proceedings before a referee requiring a claimant to appear at a time certain and set up his rights to a certain

fund in the custody of the bankruptcy court, is a plenary and not a summary proceeding.

Compare, inferentially, *Eyster v. Gaff*, 91 U. S. 525, cited in *Bardes v. Bank*, 4 A. B. R. 171, 174 U. S. 524. Also, compare, *Boyd v. Glucklich*, 8 A. B. R. 397, 116 Fed. 131 (C. C. A. Iowa). Compare, *In re Rochford*, 10 A. B. R. 611, 124 Fed. 182 (C. C. A. S. Dak.).

fendants' rights have been protected as substantially as if the suit had been plenary. In order that proceedings to recover property may be validly commenced by petition in bankruptcy, the petition must, as was suggested in *Milner v. Meek*, 95 U. S. 252, 257, 24 L. Ed. 444, contain a complete statement of the cause of action, and a sufficient prayer for relief. Upon such a petition process must be issued, and the parties must be given full opportunity to present evidence and arguments in their own behalf. In other words, though the formal requisites of a bill in equity may be wanting, yet the substantial requisites of equitable justice must be complied with as fully in a petition in bankruptcy as in a bill in equity. An injunction should not issue *ex parte*, unless in case of necessity. An order to show cause should precede the issuance unless the petitioner shows that delay will work irreparable injury. In this case it appears that all substantial requirements were met. Originally, it is true, an injunction was issued *ex parte*, but that may have been done because the referee deemed that irreparable injury would be wrought by delay. In any event, that preliminary injunction is not now in question. All parties were given full opportunity to introduce evidence and present arguments, and they seem to have availed themselves of the opportunity."

But compare, *contra*, *obiter*, *In re Connolly*, 3 A. B. R. 842, 100 Fed. 620 (Ref. Pa.): "Another objection made was that the proceedings deprived the respondent of his property by summary process. The referee cannot find that a proceeding by petition and answer is a summary process. A petition duly answered and followed by proof, has the full force and effect of a bill in equity. In the case of *Milner v. Meek*, 95 U. S. 252, 24 L. Ed. 444, the effect of pleadings by petition and answer in a bankrupt suit are discussed. Chief Justice Waite, in giving the opinion of the court, states: 'The pleading filed by the assignee was appropriate in form for a petition in the bankrupt suit, but it was equally good in substance as a bill in equity. It contains a complete statement of the cause of action cognizable in equity, and a sufficient prayer for relief.' * * *

"In *Stickney v. Wilt*, 23 Wall. 150, 23 L. Ed. 50, the petition was in all its essential features like the one in the case above—*Milner v. Meek*. It was filed by an assignee in bankruptcy against lien creditors entitled as of the bankrupt suit, and addressed to the district judge. Like that in the case above it contained no formal prayer for a subpoena, but there was a prayer for relief. 'The petition contained every requisite of a good bill in equity, whether the pleadings be tested by the statement of the cause of action, or of the charging part of the bill, or by the prayer for relief.' Opinion by Clifford, J.

"A proceeding is summary where an order is made on the petition alone, as was the case in *In re Abraham* (2 Am. B. R. 266), 35 C. C. A. 592, 93 Fed. 767, previously cited; but where an answer to a petition is filed, and proof taken, respondent is not deprived of any right that he would have had if more formal proceedings by bill of equity had been instituted." It must be noted in this case however that the court had jurisdiction over the *rem* as well as by consent, and so summary proceedings were proper.

§ 1833. Summary Orders to Surrender Assets Not New Function.

—It is no new function for courts of equity to require surrender of property by bankrupts and others not claiming adversely: courts of equity have always had the power.²⁴

²⁴ *In re Purvine*, 2 A. B. R. 787, 96 Fed. 192 (C. C. A. Tex.). *Impliedly*, *In re Rosser*, 4 A. B. R. 156, 101 Fed. 653 (C. C. A. Mo.).

In re Cotton Co., 14 A. B. R. 197, 134 Fed. 477 (D. C. Ark.): "These provisions in the Bankruptcy Act, authorizing courts of bankruptcy to enforce obedience to their orders by punishment as for contempt are neither novel nor unusual. They were included in every Bankruptcy Act, and similar provisions have been enacted by almost every State in the Union, including the State of Arkansas. In proceeding supplemental to or in aid of executions, courts are authorized by these statutes to enforce the surrender of assets subject to execution, and for this purpose may commit to jail any person refusing to comply with such order."

Inferentially, In re Holland, 23 A. B. R. 835, 176 Fed. 624 (D. C. N. Y.): "The situation is much similar to that existing in proceedings supplementary to execution upon a judgment in a court of law, where authority is given by statute to impose a fine equal to the amount of the execution, with costs, and to imprison the party in contempt until the fine is paid."

§ 1834. Right of Trial by Jury Not Violated Thereby.—The right of trial by jury is not violated by summary process.

Ripon Knitting Wks. v. Schreiver, 4 A. B. R. 300, 101 Fed. 810 (D. C. Wash.): "As a court of bankruptcy, this court is a special tribunal, and when a case proceeds according to the usual practice in courts of bankruptcy a party against whom a decision is rendered has no more right to complain of being deprived of his rights without due process of law than have parties against whom judgments are rendered in equity or admiralty cases."

§ 1835. Bankrupt Ordered to Execute Necessary Papers.—The bankrupt may be ordered to execute assignments, applications and other papers necessary to obtain possession or title.²⁵

O'dell v. Boyden, 17 A. B. R. 759, 150 Fed. 731 (C. C. A. Ohio): "Only through a court of equity can the pecuniary value of such an asset be realized to creditors or assignees. Only by decree in personam compelling the bankrupt member, can such a transfer of membership be effectuated as will put the buyer in the place of Henrotin as a member. Over him for that purpose the bankrupt court has exclusive control, and, in this sense, also, may it be said, that the 'seat' or 'membership' was in custodia legis when the trustee sought the aid of the court to adjudicate the claims and liens asserted by O'Dell."

Obiter, In re Granite City Bk., 14 A. B. R. 407, 137 Fed. 818 (C. C. A. Iowa). "As to property without the domain of the National Act, § 7, subd. 5, requires the bankrupt to execute transfers thereof to the trustee in bankruptcy."

In re Wiesel & Knaup, 23 A. B. R. 59, 173 Fed. 718 (D. C. Pa.): "This license the receiver advertised and sold, and it is the duty of the bankrupts to assist the receiver in securing a transfer to the purchaser, so far as they are able to

²⁵. See ante, §§ 460, 969, 1009, 1115; In re Hurlbut, 13 A. B. R. 50, 135 Fed. 504 (C. C. A. N. Y.), quoted at § 1115; In re Becker, 3 A. B. R. 412, 96 Fed. 407 (D. C. Pa.); In re Eurich, 4 A. B. R. 89, 101 Fed. 231 (D. C. Pa.); In re Coleman, 14 A. B. R. 461, 136 Fed. 818 (C. C. A. N. Y.), quoted ante, § 1009; In re Wolff, 21 A. B. R. 452, 165 Fed. 984 (D. C. N. Y.); In re Diack, 3 A. B. R. 723, 100 Fed. 770 (D.

C. N. Y.); Fisher v. Cushman, 4 A. B. R. 646, 103 Fed. 867 (C. C. A. Mass.), quoted at § 1115; In re Wright, 18 A. B. R. 198, 292, 151 Fed. 361 (D. C. N. Y.); (1867) In re Ketcham, 1 Fed. 840; In re Madden, 6 A. B. R. 614, 110 Fed. 348 (C. C. A. N. Y.); In re Burnstine, 12 A. B. R. 596, 131 Fed. 828 (D. C. Mich.); In re Phelps, 15 A. B. R. 170 (Ref. N. Y.).

render such assistance. Up to the time of their discharge, they can be compelled, by summary order of court, to give the receiver any information they may possess or render him any assistance they can in the transfer of possession of property belonging to the bankrupt estate."

Thus, to execute assignments of rights in patents.²⁶

§ 1836. Referee Has Jurisdiction to Make Summary Order.—The referee has jurisdiction to make the summary order on bankrupts.²⁷

In *re Miller*, 5 A. B. R. 184, 105 Fed. 57 (D. C. Iowa): "Under the rule laid down in this case it is clear that the referee, upon whom is imposed the duty of collection through the trustee the property of the estate, had the right to enter an order directing the bankrupt to surrender to the trustee any money or property which the referee found to be in possession or under the control of the bankrupt, opportunity having been given to the bankrupt to be heard upon the question; and upon the refusal or neglect of the bankrupt to obey the order thus made the referee had the right to enter upon the record the fact that the bankrupt had refused obedience therefore was in contempt of the court."

In *re Mayer*, 3 A. B. R. 533, 98 Fed. 839 (D. C. Wis.): "The jurisdiction of the referee to entertain the hearing in question and to enter the order thereon is undoubted."

And also on others²⁸ not holding adversely.²⁹

Mueller v. Nugent, 184 U. S. 1, 7 A. B. R. 224 (reversing 5 A. B. R. 176 and affirming 4 A. B. R. 747): "It is now said that the only power the referee has to direct the taking possession of property is given by subsection 3 of § 38a, providing that the referee may exercise the powers of the judge in that respect on a certificate of the clerk that the judge is absent or unable to act. But that provision seems to refer only to the seizure of property by the marshal or a receiver prior to adjudication and the qualification of the trustee as provided by § 2, § 3e, and § 69, and it is at all events inapplicable here.

"We think the referee has the power to act in the first instance in matters

²⁶. In *re Cantelo Mfg. Co.*, 26 A. B. R. 57, 185 Fed. 276 (D. C. Me.).

²⁷. In *re Oliver*, 2 A. B. R. 783 (D. C. Calif.); impliedly, In *re Davis*, 9 A. B. R. 670 (D. C. Tex.); impliedly, In *re Purvine*, 2 A. B. R. 787, 96 Fed. 192 (C. C. A. Tex.); In *re Rosser*, 4 A. B. R. 153, 101 Fed. 562 (C. C. A. Mo.); impliedly, In *re Tudor*, 2 A. B. R. 808, 96 Fed. 942 (D. C. Colo.); In *re Logan*, 28 A. B. R. 543, 196 Fed. 678 (D. C. N. Y.); In *re Schimmell*, 29 A. B. R. 361, 203 Fed. 181 (D. C. Pa.); quoted at § 2841. Compare, same as to marshaling liens, etc., post, § 1888.

²⁸. *Knapp & Spencer v. Drew*, 20 A. B. R. 355, 160 Fed. 413 (C. C. A. Neb.), quoted at § 1800.

²⁹. In *re Scherber*, 12 A. B. R. 618, 131 Fed. 121 (D. C. Mass.); In *re Alphin & Lake Cotton Co.*, 12 A. B. R. 654, 131 Fed. 824 (D. C. Ark.); impliedly, In *re Feldser*, 14 A. B. R. 216,

134 Fed. 307 (D. C. Penn.); In *re Cohn*, 18 A. B. R. 786 (Ref. Calif.). Compare, same as to marshaling liens, etc., post, § 1888. Instance, In *re Kornit Mfg. Co.*, 27 A. B. R. 244, 192 Fed. 392 (D. C. N. J.); instance, In *re Hays*, 24 A. B. R. 691, 181 Fed. 674 (C. C. A. Ohio), quoted at § 1665.

As, for instance, upon an officer of a bankrupt corporation. In *re Alphin & Lake Cotton Co.*, 12 A. B. R. 780, 131 Fed. 824 (D. C. Ark.).

Impliedly, In *re Northrop*, 1 A. B. R. 427 (Ref. N. Y.), where the referee was held to have even power to issue injunctions upon court officers. This decision, however, in thus holding, goes too far. Instance, In *re Cole*, 14 A. B. R. 389 (D. C. Me., affirmed in 16 A. B. R. 302, 144 Fed. 392). But compare, *Smith v. Belford*, 5 A. B. R. 294, 106 Fed. 658 (C. C. A. Ohio).

such as this, when the case has been referred, and in aid of the court of bankruptcy, and exercises in such cases 'much of the judicial authority of that court.'"

In *re Kane*, 12 A. B. R. 445, 131 Fed. 386 (D. C. N. Y.): "If it be clearly a nullity, the referee has jurisdiction, and may by summary process require the surrender of the property so withheld to the trustee in bankruptcy."

And the referee has jurisdiction to make such summary order, even though it be an order upon a court officer.³⁰ The lack of power in the referee to enjoin courts or officers,³¹ is evidently construed not to be the same as lack of power to order the summary delivery of property by such officers.³²

§ 1837. Written Petition Requisite.—A written petition must be filed or served making specific claim to certain described property in the possession or control of the bankrupt, agent, or other party and it must be so framed as to fairly apprise such party of what he is expected to meet. Thus, as to the bankrupt.³³

Inferentially, *Boyd v. Glucklich*, 8 A. B. R. 393, 116 Fed. 131 (C. C. A. Iowa): "No petition had been filed by the trustee claiming that the bankrupt had money or property in his possession or under his control which he should turn over to the trustee."

In *re Ruos* (No. 2), 21 A. B. R. 257, 164 Fed. 749 (D. C. Pa.): "If it had appeared in the course of this inquiry that the bankrupt probably controlled or was possessed of money or property that rightfully belonged to his estate, the correct proceeding to compel delivery would have been begun by presenting a petition making definite averments upon this subject and offering a definite issue. To such a petition the bankrupt would have been entitled to reply, and upon the issue raised by his answer both parties would have had the right to offer evidence, not only that which had been already taken, but such further evidence as might be relevant. The facts would thus appear, and the proper order would have the necessary support. Here, however, there was neither an appropriate petition nor an answer thereto, and therefore no issue to which the evidence can be definitely applied. On such a record I must decline to make an order that might be followed by the imprisonment of the bankrupt."

In *re Lasch*, 12 A. B. R. 158 (Ref. Penn.): "* * * A distinct issue must be raised upon petition and answer and testimony must be taken thereunder."

^{30.} In *re Cohn*, 18 A. B. R. 786 (Ref. Calif.); impliedly, upon the facts, In *re Geiser*, 12 A. B. R. 208 (D. C. Mont.); inferentially, In *re Huddleston*, 1 A. B. R. 572 (Ref. Ala.).

Compare, however, *Smith v. Belford*, 5 A. B. R. 294, 106 Fed. 658 (C. C. A. Ohio, affirming the doctrine of In *re Nugent*, 5 A. B. R. 176, afterwards reversed in *Mueller v. Nugent*, 184 U. S. 1).

Inferentially, In *re Thompson*, 11 A. B. R. 719, 128 Fed. 575 (C. C. A. N. Y.), in which case the Circuit Court of Appeals sustained a referee's summary order on an assignee who had voluntarily appeared in the first instance and later claimed to be an adverse party as to certain items.

Compare, also, as to the point that the taking of property out of one's possession and the restraining such one's use of it are but different acts of the exercise of the same jurisdiction, In *re Ward*, 5 A. B. R. 215, 104 Fed. 985 (D. C. Mass.).

^{31.} See ante, "Functions of Referees," §§ 539, 540, et seq.

^{32.} Contra, In *re Ward*, 5 A. B. R. 215, 104 Fed. 985 (D. C. Mass.).

^{33.} In *re Pearson*, 2 A. B. R. 819, 95 Fed. 425 (Ref. Penn.); inferentially, In *re Oliver*, 2 A. B. R. 783 (D. C. Calif.); impliedly, In *re Schachter*, 9 A. B. R. 499 (D. C. Ga.); In *re Frank*, 25 A. B. R. 486, 182 Fed. 794 (C. C. A. N. D.).

Thus, as to a court officer.³⁴

Obiter and inferentially, *Louisville Trust Co. v. Comingor*, 184 U. S. 18, 7 A. B. R. 426. "Nor in this matter was any petition by the trustee, or by any other person, filed against *Comingor* to recover these sums, and the orders were entered by the referee on the record as it stood, so that there was no pretense whatever of a plenary suit in that court, in form or in substance.

"The proceeding was purely summary."

Thus, as to a mortgagee who has (though under mistaken advice of counsel) waived title to goods under the mortgage, and yet receives the same from the receiver in bankruptcy and is ordered to surrender them.³⁵ But the description of the property need be no more particular than the nature of the case permits of.³⁶

Ripon Knitting Works v. Schrieber, 4 A. B. R. 303, 101 Fed. 810 (D. C. Wash.): "The principles of reason and justice do not exact of those who have incurred losses by extending credit to a dishonest merchant the impossible thing of tracing the proceeds of merchandise which he had handled before compelling him to surrender money in his possession which rightfully should be applied to the payment of their accounts. In this case it is impossible for the trustee or the creditors to identify the pieces of money which have come to the bankrupt's hands, or to identify or describe the particular pairs of shoes which were sold for money which the bankrupt now conceals; and, being impossible, it is unnecessary."

The petition must be filed in the trustee's name.³⁷

In *re Rothschild*, 5 A. B. R. 587 (D. C. Ga.): "The nature of the proceedings does not change the rule. All proceedings must be brought by or against the trustee, except such proceedings as affect one individual creditor or one class of creditors only."

If the averments of the petition are indefinite or uncertain, the proper remedy is by motion, or some other appropriate request, that it be made more definite and certain.³⁸

Demurring and answering to the petition at the same time effects a waiver of the demurrer.³⁹

§ 1838. Reasonable Notice on Respondent, Requisite.—Reasonable notice must be served on the bankrupt or other party upon whom the

34. *Bear v. Chase*, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S. Car.). Compare, practice, *In re Hecox*, 21 A. B. R. 314, 164 Fed. 823 (C. C. A. Colo.). Compare, practice, *Hooks v. Aldridge*, 16 A. B. R. 664, 145 Fed. 865 (C. C. A. Tex.).

35. Inferentially (matter of contempt.), *In re Cole*, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.).

36. Compare, as to extent of proof requisite, *In re Jackier*, 24 A. B. R. 790, 179 Fed. 720 (D. C. Pa.).

37. *In re Carter*, 1 N. B. N. 162 (Ref.); *In re Pearson*, 2 A. B. R. 819, 95 Fed. 425 (Ref. Penn.). See ante, "After Trustee Elected, All Objections, etc., to Be by Him or in His Name," § 824; post, "All Proceedings to Be Taken in Trustee's Name," § 2827.

38. *In re Frank*, 25 A. B. R. 486, 182 Fed. 794 (C. C. A. N. D.).

39. Compare, § 331½; also see *In re Koplin*, 24 A. B. R. 534, 179 Fed. 1013 (D. C. Pa.).

order is requested, so that he may have reasonable time to prepare for his defense.⁴⁰

In *re Rosser*, 4 A. B. R. 153, 101 Fed. 562 (C. C. A. Mo., reversing 2 A. B. R. 746): "A more serious question is presented by the contention of the bankrupt, that the proceedings in the court below did not give him such a notice of, and such an opportunity to be heard upon, the propriety of the order for the payment of his money as constitute due process of law. Chancellor Kent says: 'The better and larger definition of "due process of law" is that it means law in its regular administration through courts of justice.' 2 Kent, Comm. 13. While it is perhaps impossible, and is certainly unwise, to attempt to give a concise and comprehensive definition of the term 'due process of law' and 'law of the land,' it is certain that notice to the party to be affected of the claim against him, and an opportunity to be heard upon it, are essential elements of every proceeding in a court of justice which can be said to constitute due process of law or to be in accord with the law of the land. 'Perhaps no definition,' says Judge Cooley, 'is more often quoted than that given by Mr. Webster in the *Darmouth College Case*: "By 'law of the land' is most clearly intended the general law; a law which hears before it condemns, which proceeds upon inquiry and renders judgment only after trial. The meaning is that every citizen shall hold his life, liberty, property, and immunities under the protection of the general rules which govern society.'" Cooley, *Const. Lim.* 431. The basic principle of English jurisprudence is that no man shall be deprived of life, liberty or property without due process of law, without a course of legal proceedings according to those rules and forms which have been established for the protection of private rights. Such a course must be appropriate to the case and just to the party affected. It must give him notice of the charge or claim against him, and an opportunity to be heard respecting the justice of the order or judgment sought. The notice must be such that he may be advised from it of the nature of the claim against him, and of the relief sought from the court if the claim is sustained. And the opportunity to be heard must be such that he may, if he chooses, cross-examine the witnesses produced to sustain the claim, and produce witnesses to refute it, if a question of fact is in issue, and, if a question of law is presented, the opportunity to be heard must be such that his counsel may, if they desire, argue the justice and propriety of the judgment or order proposed. Judicial orders or judgments affecting the lives or property of citizens in the absence of such a notice and opportunity to the party affected are violative of the fundamental principles of our laws, and cannot be sustained. * * * Under the principle to which reference has been made, he was entitled to a citation or notice of a hearing upon this claim and of the proposed order before it was made. * * * No order to show cause why he should not pay it was made or served upon him before the absolute order for its payment was presented to him. No opportunity was afforded him to be heard upon the questions it presents. He was cited to appear and be examined under § 21 of the Bankrupt Act, and his testimony and that of various other witnesses were taken before the referee upon that citation, but no notice was served upon him that the claim, which culminated in the order for the payment of the \$2,500, was made or was in issue at that examination, or that the testimony there elicited was taken for the purpose of establishing that claim,

⁴⁰ In *re Pearson*, 2 A. B. R. 819, 95 Fed. 425 (Ref. Penn.); In *re Miller*, 5 A. B. R. 184, 105 Fed. 57 (D. C. Iowa); In *re Oliver*, 2 A. B. R. 783,

96 Fed. 85 (D. C. Calif.); In *re Schachter*, 9 A. B. R. 499 (D. C. Ga.). Impliedly, In *re DeGottardi*, 7 A. B. R. 728, 114 Fed. 328 (D. C. Calif.).

and no opportunity was presented to him to produce witnesses in his defense or to be heard upon the issues of fact or of law which the issue of the order involved. Such a proceeding lacks every element of due process of law. It contains no notice to the party affected of the claim against him, or of the proposed action upon it, no opportunity to contest the questions of fact which it presents by the cross-examination of the claimant's witnesses or the presentation of his own, and no chance to be heard upon the questions of law which it involves. It considers without notice, condemns without hearing, and renders judgment without trial."

In *re Frank*, 25 A. B. R. 486, 182 Fed. 794 (C. C. A. N. D.): "It is true that the case before us differs from the *Rosser* case in that the petitioner here was given two days' notice of the hearing upon the petition filed by the trustee. But that petition was based upon alleged disclosures of the petitioner when under examination before the petition was filed, and when he had no notice that his examination was to be used or would be used upon the hearing of the petition that was subsequently filed; and afterwards further testimony was taken to be used against him upon the hearing, no notice of the taking of which was given and no opportunity afforded him to appear and cross-examine the witnesses; in fact it appears that the petitioner was detained at Minot, N. D., by order of the referee at the instance of the trustee while such testimony was being taken. It therefore clearly appears that the order of the referee deprived the petitioner of his legal rights, and in respect of the taking of the testimony is in effect the same as the order in *Re Rosser*."

Boyd v. Glucklich, 8 A. B. R. 393, 116 Fed. 131 (C. C. A. Iowa): "Dispatch in judicial proceedings is commendable but in proceedings involving the liberty of a citizen, he has a right not only to be informed of the precise claim against him, but, after receiving that information, he has a right to a reasonable time to prepare his answer and present his proofs, and, lastly, to be heard by counsel on the law and facts of the case. While proceedings in bankruptcy may be summary, they should not be too summary; in other words, they should not be so summary as to deprive the bankrupt of those fundamental rights and privileges that belong to every citizen, among which are the right to be advised of the demand made upon him, and the right, after being so advised, to have a reasonable time to prepare his defense and produce his witnesses. The Bankrupt Act does not do away with these rights, and no citizen forfeits them by being adjudged a bankrupt. The Bankrupt Act contemplates that proceedings in bankruptcy shall go forward with all reasonable dispatch compatible with the due and orderly administration of justice and a proper regard for the fundamental rights of the citizen. Construing the proceedings before the referee as we do, we think they were too summary in their character, and that it was against this summary proceeding the bankrupt asked to be heard, and that there was not accorded to him, and not intended to be accorded to him, by the referee, a reasonable time to answer the trustee's application, or to be further examined or to introduce evidence after being advised of the specific claims made against him by the trustee. The referee did not advise him that he had these rights, and the record does not show that he waived them, or intended to do so. As we construe the record, this case is not, in this respect, different from that of *In re Rosser*, 4 Am. B. R. 153, 41 C. C. A. 497, 101 Fed. 562. It is true that in that case the referee made the order based on the bankrupt's general examination in his absence, but it is manifest from the opinion in the case that if the order had been made, as it was in this case, at the conclusion of a long and desultory examination, and the bankrupt heard only in a vain protest against such summary action, the result would have been the same."

Thus, notice must be served on an assignee or receiver from whom surrender is demanded.⁴¹

§ 1838½. Order to Show Cause.—The ordinary notice is that of an “order to show cause.”⁴³

In *re Burkhalter & Co. (Rogers v. People's Bank)*, 24 A. B. R. 553, 179 Fed. 403 (D. C. Ala.): “The petition prays for a rule upon the respondent to show cause why the money should not be restored to the fund by the respondent. This has the effect of bringing the respondent into court.”

No notice of the granting of the order to show cause itself is necessary, however.

In *re (Philip) Brady*, 21 A. B. R. 364, 169 Fed. 152 (D. C. Ky.): “While a notice might not have been improper, it was not at all necessary because the show-cause order itself gives notice and affords an opportunity on a certain named future day to show cause why the special relief sought should not be granted. The order, *per se*, gives him his day in court.”

The order to show cause on a summary petition to surrender assets may not run into another district; for whilst it is true that the bankruptcy court of one district in possession of a *res* may issue a citation upon a party in another district to show cause why certain contemplated action in relation to the *res* should not be taken, yet it is quite another thing to issue process to be affirmatively enforced in the other jurisdiction, such as a summary order requiring a third party to do or abstain from doing a certain thing.⁴⁴

§ 1839. Due Hearing Requisite.—Due hearing must be had, and reasonable opportunity therefor is requisite.⁴⁵

Boyd v. Glucklich, 8 A. B. R. 397, 116 Fed. 140 (C. C. A. Iowa): “The alleged contempt in this case was not committed in the presence of the court, and is therefore what the law denominates a ‘constructive contempt.’ It is a criminal offense for which the punishment may be imprisonment without limit of duration, and one charged with it has the same inalienable right to be heard in his defense that he would if charged with murder or any other crime. In *Ex parte Robinson*, 19 Wall. 505—a proceeding to punish for contempt—the Supreme Court said:

“There may be cases, undoubtedly, of such gross and outrageous conduct in

41. *Smith v. Belford*, 5 A. B. R. 294, 106 Fed. 658 (C. C. A. Ohio); *Loveless v. Southern Grocer Co.*, 20 A. B. R. 180, 159 Fed. 415 (C. C. A. La.).

43. See post, §§ 1890, 1982.

44. *Staunton v. Wooden*, 24 A. B. R. 736, 179 Fed. 61 (C. C. A. Cal.), quoted at § 1705¼.

45. In *re Rosser*, 4 A. B. R. 153, 101 Fed. 562 (C. C. A. Mo.); In *re Pearson*, 2 A. B. R. 819, 95 Fed. 425 (Ref. Penn.); *obiter*, *Ripon Knitting Wks. v. Schreiber*, 4 A. B. R. 299, 101 Fed. 810 (D. C. Wash.); In *re Frank*, 25 A. B. R. 486, 182 Fed. 794 (C. C. A. N.

D.); In *re Soloway & Katz*, 28 A. B. R. 225, 196 Fed. 132 (D. C. Conn.); analogously, instance where summary order on receiver to surrender property in his possession was refused too summarily, In *re Corn*, 24 A. B. R. 681, 179 Fed. 841 (C. C. A. N. Y.); *Loveless v. Southern Grocer Co.*, 20 A. B. R. 180, 159 Fed. 415 (C. C. A. La.), quoted at § 1611½. As to what was not lack of reasonable notice and due hearing, see In *re Friedman*, 20 A. B. R. 37, 161 Fed. 260 (C. C. A. N. Y.).

open court on the part of the attorney as to justify very summary, proceedings for his suspension or removal from office; but even then he should be heard before he is condemned. The principle that there must be citation before hearing, and hearing or opportunity of being heard before judgment, is essential to the security of all private rights. Without its observance, no one would be safe from oppression wherever power may be lodged.'

"And this was said in a case where the alleged contempt was committed in the presence of the court."

Thus, a party's own testimony taken on general examination, whether reduced to writing or verbally testified to, is admissible (but admissible only) in proceedings directed against the particular bankrupt or witness who has given the testimony and against whom relief is sought.⁴⁶ This rule applies to the officers of a bankrupt corporation.⁴⁷

But the testimony of other witnesses, although taken on general examination, is not admissible against the bankrupt or other witness;⁴⁸ except so far, of course, as any witness may be confronted with former contradictory statements for the purpose of discrediting him.

In *re Alphin & Lake Cotton Co.*, 12 A. B. R. 655, 131 Fed. 824 (D. C. Ark.): "But does this rule apply to the deposition of Smith (a third party) * * *. We are therefore called upon to determine whether the testimony of a person other than the bankrupt, or, in case of a bankrupt corporation, not an officer or member thereof, taken and reduced to writing under the provisions of § 21a of the Bankruptcy Act, before any proceedings to require the parties against whom the testimony is to be used to show cause had been instituted, is admissible as evidence in a proceeding of this kind against the bankrupt, or, if the bankrupt is a corporation, against its officers. * * * As a general rule, depositions of witnesses taken in a former suit pending between one of the parties and a party other than the opponent in the last-trying action, cannot be read in evidence at the trial of the latter suit, even if there has been cross-examination, nor, for that matter, if the parties to both actions were the same, but the issues involved or objects sought to be attained in the two suits were different—especially if the witness was competent to testify in the last action, and could have been used by the party as such."

The bankrupt, or other party proceeded against, may introduce evidence in his own behalf.⁴⁹ Where a party has had an opportunity to call and ex-

46. See ante, "Discovery of Assets," § 1555. In *re Alphin & Lake Cotton Co.*, 12 A. B. R. 653, 131 Fed. 824 (D. C. Ark., affirmed by C. C. A., 14 A. B. R.); In *re Weissen Bros.*, 14 A. B. R. 347, 135 Fed. 442 (D. C. Penn.); analogously, In *re Dow*, 5 A. B. R. 400, 105 Fed. 889 (D. C. Iowa); analogously, In *re Gaylord*, 7 A. B. R. 1, 111 Fed. 717 (C. C. A. N. Y., affirming 5 A. B. R. 410). See ante, "Discovery of Assets," § 1555. Also, see § 1747.

47. In *re Alphin & Lake Cotton Co.*, 12 A. B. R. 653, 131 Fed. 824 (D. C. Ark.). See also, *supra*, § 1555.

48. See ante, "Discovery of Assets,"

§ 1555. In *re Wiesen Bros.*, 14 A. B. R. 347, 135 Fed. 442 (D. C. Penn.). Contra, In *re Wilcox*, 6 A. B. R. 362, 102 Fed. 628 (C. C. A. N. Y., reversed on rehearing, 14 A. B. R. 347); contra, In *re Cooke*, 5 A. B. R. 434, 109 Fed. 631 (D. C. N. Y., following In *re Wilcox*, 6 A. B. R. 362); Inferentially, contra, In *re Leinweber*, 12 A. B. R. 175, 128 Fed. 641 (D. C. Conn.); inferentially contra, In *re Alder*, 12 A. B. R. 19, 129 Fed. 502 (D. C. Tenn.).

49. In *re Lasch*, 12 A. B. R. 158 (Ref. Penn.); inferentially, In *re Miller*, 5 A. B. R. 184, 105 Fed. 57 (D. C. Iowa); *Boyd v. Glucklich*, 8 A. B. R. 397, 116

amine his witnesses and the matter is closed, he should not be permitted to reopen the case for the introduction of evidence which he subsequently concludes would have been an advantage to him, unless for special reasons.⁵⁰

It often occurs, that, during the midst or at the end of a general examination of the bankrupt, and especially when some particularly flagrant and incredible statement, or some telling admission has been made by the bankrupt in his testimony, the trustee's attorney arises in indignation and demands that the court issue a peremptory order upon the bankrupt to turn over to the trustee at once the certain property then under discussion. This must not be done, however.

§ 1840. Courts Proceed with Great Caution in Granting Summary Orders.—Courts exercise this power of ordering the turning over of property with the greatest caution, lest the imprisonment for contempt which would follow the failure to comply with an order to turn over property might rather amount to imprisonment for debt.⁵¹

Samel v. Dodd, 16 A. B. R. 167, 142 Fed. 68 (D. C. Ga.): "While bankruptcy courts are invested with power, as we have already shown, to require bankrupts to surrender their property and to enforce obedience to the order by attachment for contempt, yet 'the power is far-reaching and drastic and should be exercised with cautious discretion.' Indeed, it may be said that it should never be exercised, except in a plain case, and always with a due regard to the constitutional rights of the citizen. In this immediate connection the apt words of Mr. Justice Bradley may be appropriately employed: 'It is the duty of the courts to be watchful for the constitutional rights of the citizen and against any stealthy encroachments thereon. Their motto should be "Obsta principiis."' *Boyd v. U. S.*, 116 U. S. 635. It is objected, however, that the failure of courts to exercise with a firm hand the power to punish by contempt proceedings, designing and unscrupulous bankrupts would practicably deprive the law of its efficacy and convert it into a mere shield for the protection of dishonest debtors. In doubtful cases the power should not be exerted; and in view of the stringent provisions of law punishing fraudulent conduct and other forms of dishonesty on the part of the bankrupt, the objection is untenable. The original act not only contains ample provisions for the punishment of the bankrupt in the regular mode of trial by jury, for false swearing and for the fraudulent disposition of assets (§ 29), but § 14, as amended by the act of February 5, 1903, renders it extremely difficult, if not impossible, for the contumacious or dishonest bankrupt to secure a discharge from his indebtedness."

In *re Lesaius*, 21 A. B. R. 23, 163 Fed. 614 (D. C. Pa.): "No doubt in cases of this kind an order is not to be made except with caution and upon convincing evidence, lest a commitment for disobedience on contempt proceedings to follow should in effect be nothing more than imprisonment for debt."

No person may be imprisoned for debt on process issued from the courts

Fed. 140 (C. C. A. Iowa); In *re Ruos* (No. 2), 21 A. B. R. 257, 164 Fed. 749 (D. C. Pa.), quoted at § 1837.

⁵⁰ In *re Booss*, 18 A. B. R. 658, 154 Fed. 494 (D. C. Pa.), quoted at § 553½.

⁵¹ In *re Mize*, 22 A. B. R. 577, 172 Fed. 945 (D. C. Ala.). Compare, to similar effect, In *re Jackier*, 24 A. B. R. 790, 179 Fed. 720 (D. C. Pa.), quoted at § 1842.

of the United States in a State whose laws prohibit imprisonment for debt.⁵² Imprisonment for debt in most States has been abolished, and, at any rate, is conceded to be contrary to our policy, and courts will be exceedingly careful that an order upon a debtor to turn over assets does not degenerate into an order to pay when the debtor has not the means to pay, which would result in nothing less than imprisonment for debt were the order to be followed by commitment for contempt.⁵³

Boyd v. Glucklich, 8 A. B. R. 393, 116 Fed. 140 (C. C. A. Iowa): "A court of bankruptcy cannot sentence a bankrupt to imprisonment for debt, any more than any other court of the United States can do that thing; and what it cannot do directly it cannot do by indirection, under another name. It cannot, therefore, lawfully order a bankrupt to deliver to the trustee money or property he has not got in his possession or under his control, and imprison him if he does not comply with the order. Plainly, that would be imprisonment for debt, and the order is not relieved of that illegal and odious quality by calling it 'imprisonment for contempt.' The court that makes such an order is in contempt of the law and constitution, and not the bankrupt in contempt of the court."

Compare, to same effect, *Trust Co. v. Wallis*, 11 A. B. R. 364, 126 Fed. 464 (C. C. A. Pa.): "An order made under such circumstances would be as absurd as it is inconsistent with the principle of individual liberty."

In *re Holland*, 23 A. B. R. 835, 176 Fed. 624 (D. C. N. Y.): "But the more serious question is whether the contempt of court has been willful, and whether there is ability to repay, because, in the absence of either of these elements, an order directing punishment for contempt, by compelling the payment in indebtedness through the compulsion of imprisonment (it being apparent that, if the person in contempt is unable to pay, the money to release him must be raised by other people), would be perilously close to imprisonment for debt or crime, and no authority for that method of collection can be found under the laws of the United States."

In *re Dickens*, 23 A. B. R. 660, 175 Fed. 808 (D. C. Ala.): "This proceeding cannot be invoked as a means of coercing payment of debts, or to punish the bankrupt for transferring his property with the intent to hinder, delay, or defraud his creditors, if such be the fact."

In *re Marks*, 23 A. B. R. 911, 176 Fed. 1018 (D. C. Pa.): "Unless he has the physical ability to comply, he should not be committed for contempt; in practical effect, although perhaps not in legal contemplation, this would revive the abolished penalty of imprisonment for debt."

§ 1841. Punishment for Disobedience of Summary Order, Not Imprisonment for Debt.—But punishment for contempt for failure to turn over property found to be in the possession of the party proceeded

⁵² U. S. Rev. Stats., § 990; In *re Blanche Page*, 16 Blatchf. 1, Fed. Cas., No. 1,524; *Mfg. Co. v. Fox*, 20 Fed. 409.

⁵³ In *re McCormick*, 3 A. B. R. 340, 97 Fed. 566 (D. C. N. Y.); *Sinsheimer v. Simonson*, 5 A. B. R. 546, 107 Fed. 898 (C. C. A. Ky.), affirmed sub nom. *Louisv. Trust Co. v. Cominger*,

7 A. B. R. 421, 184 U. S. 18; impliedly, In *re Adler*, 12 A. B. R. 21, 129 Fed. 502 (D. C. Tenn.); In *re Ogles*, 2 A. B. R. 514 (Ref. Tenn.). Compare, to same effect, In *re Purvine*, 2 A. B. R. 787, 96 Fed. 192 (C. C. A. Tex.).

In *re Lesaius*, 21 A. B. R. 23, 163 Fed. 614 (D. C. Pa.). Compare, analogously, post, § 2339.

against does not violate the prohibition against imprisonment for debt.⁵⁴

In *re Rosser*, 4 A. B. R. 157, 158, 101 Fed. 562 (C. C. A. Mo.): "The contention that the commitment of a contumacious bankrupt to jail until he complies with such an order constitutes imprisonment for debt, and is prohibited by the constitution of Missouri, is untenable. Such an order is not an order for the payment of a debt. All the property of the bankrupt estate is placed in custodia legis by the adjudication in bankruptcy. Every part of the estate belongs to the court, and vests in the trustee when appointed, and the bankrupt and every other party who has the possession or control of any part of it holds that part as the agent and trustee of the court and its officer. The money or the property of the estate which a bankrupt thus holds is not a debt which he owes to the court or to the trustee, but it is the money or property of the court or of the trustee, which it is alike the duty of the court, of the referee, and of the bankrupt to place in the hands of the trustee in bankruptcy for distribution to the creditors pursuant to the provisions of the bankruptcy law. An order for the payment of money or the delivery of property, which is a part of the estate in bankruptcy, and which is in the control and possession of the party directed to pay or deliver it, at the time of the making of the order, is not an order for the payment of a debt, and a commitment to jail until such order is complied with is not imprisonment for debt, under section 16, article 2, of the constitution of Missouri, and section 8954 of the Revised Statutes of that State."

Schweer v. Brown, 12 A. B. R. 178, 130 Fed. 328 (C. C. Ark., affirmed in 12 A. B. R. 673, 195 U. S. 171): "The first contention of the bankrupt is that the enforcement of the order of the District Court would constitute imprisonment for debt, and would therefore be in contravention of the provision of the Constitution of Arkansas (Const. art. 3, § 16) that no person shall be imprisoned for debt in any civil action on mesne or final process unless in case of fraud. This is no longer a debatable question. Assuming the correctness of the finding of the referee and of the District Court that the bankrupt had in his possession property belonging to his estate in bankruptcy, his obligation to comply with the order of the court by surrendering it to the trustee is not the obligation to pay a debt. The adjudication in bankruptcy operated to transfer to the trustee the title to all of the property of the bankrupt which was subject to distribution among his creditors. His obligation and his duty to surrender to the trustee property in his possession which belongs to the trustee, and not to him, cannot be converted into a debt, at his option, by his mere refusal to comply with the order of the court."

In *re Schlesinger*, 4 A. B. R. 361, 97 Fed. 930 (C. C. A. N. Y., affirming 3 A. B. R. 342): "The answer to this objection is that the order was not for the payment of a debt, but for the delivery by the bankrupt of the assets of his estate to his trustee in bankruptcy. He was not indebted to the trustee. The money was a part of his assets and estate, which had, by operation of law, become vested in the trustee; and, while the order in this class of cases is for the delivery of the bankrupt's property to the trustee, it is in no proper sense a judgment or decree for the payment of a debt. If the enforcement of an order for the delivery to the trustee in bankruptcy of the assets of an estate which had been converted into money could not be had except by an execution, the power of a bankruptcy court would be minimized, and the assets of estates in bankruptcy would be subject to great reduction."

⁵⁴ In *re Anderson*, 4 A. B. R. 640, 103 Fed. 854 (D. C. S. C., reversed, on other grounds, *McGahan v. Anderson*, 7 A. B. R. 64, 113 Fed. 115); In *re Holland*, 23 A. B. R. 835, 176 Fed. 624 (D.

C. N. Y.). Also, see *Ripon Knitting Works v. Schreiber*, 4 A. B. R. 299, 101 Fed. 810 (D. C. Wash.). Compare, inferentially, In *re Cotton Co.*, 14 A. B. R. 194, 134 Fed. 477 (D. C. Ark.).

Samel v. Dodd, 16 A. B. R. 167, 142 Fed. 68 (C. C. A. Ga.): "The order to pay over money or to surrender other property as the case may be, in the possession, of the bankrupt and forming part of his estate, is not an order for the payment of a debt, but an order for the surrender of assets placed in custodia legis by the adjudication; and his commitment upon refusing to comply with the order is not imprisonment for debt."

In *re Friedman*, 18 A. B. R. 712, 153 Fed. 939 (D. C. N. Y., affirmed in 20 A. B. R. 37, C. C. A.): "The opposition to the punishment of the persons proceeded against for contempt is really based upon a proposition perfectly sound in itself, but, I think, inapplicable to the matter in hand. A person who has no money should not be punished for contempt in failing to turn over money. But the very point of this proceeding is that it is the opinion of the court that the persons proceeded against have the money and do not tell the truth when they assert their inability to pay. Instances are numerous where this same objection was made in limine, and the court became satisfied in time, either that the parties incarcerated had spent the money, or intrusted it to still other persons who had made away with it, and thereupon the prisoners were released. But if any person into whose possession money is traced can avoid the legitimate consequence of the possession of that money by swearing that he no longer has it, or never had it, the administration of justice would become a farce."

Imprisonment for contempt for failing to surrender property found to be in one's possession is not imprisonment for debt. The party proceeded against also may be punished by commitment for contempt of court for disposing of assets which, by law, he was required to hold for creditors,⁵⁵ but that is wholly different from committing him for failure to turn them over. He should not be committed for contempt of court in failing to obey an order he no longer is able to obey, no matter how great may be his culpability in thus rendering himself incapable of complying with the order. This distinction is of importance, for his commitment in the one instance properly would be until he turned over the assets, no matter how long he might be in arriving at the point of surrender, whilst in the other instance the court, properly, would fix a definite period for the commitment.⁵⁶

The court, in *In re Taylor*, 7 A. B. R. 410, 114 Fed. 607 (D. C. Colo.), released a bankrupt who had been committed for failure to obey an order to turn over assets, after he had been imprisoned for a month, evidently becoming convinced that whilst the bankrupt ought to have assets he did not in fact have them, the court saying:

"In a proceeding of this kind the court is not authorized to imprison a bankrupt indefinitely, especially when it is not certainly known that he has the money which he is called upon to surrender, and upon the ground that the bankrupt has been kept a sufficient time, probably, to induce him to surrender the money if he has it. I suppose he must now be discharged. In making such an order

55. Thus, where the bankrupt squandered assets after notice of the filing of a bankruptcy petition against him. In *re Smith*, 26 A. B. R. 399, 185 Fed. 983 (D. C. N. Y.). Also, see *In re Tudor*, 4 A. B. R. 78, 100 Fed. 796 (D. C. Colo.).

56. See post, "Distinction between Civil and Criminal Contempt," §

2330½; also see *Gompers v. Buck Stove & Range Co.*, 221 U. S. 418, quoted at § 2330½; In *re Kahn*, 30 A. B. R. 322, 204 Fed. 581 (C. C. A. N. Y.), quoted at § 2330½; In *re Star Spring Bed Co.*, 30 A. B. R. 208, 203 Fed. 640 (C. C. A. N. J.), quoted at § 2330½.

I would not have it understood that I am at all convinced that he has not this money in some place of concealment."

The language of the court just quoted would seem to indicate an incorrect conception of the rule. The court should not have ordered the imprisonment in the first instance when it was *not certainly known that the bankrupt had the money*.

Stuart v. Reynolds, 29 A. B. R. 412, 204 Fed. 711 (C. C. A. Ala.): "When the contemnor is ordered to do the impossible, and this appears from the record, his commitment for failure to obey is arbitrary and illegal; and the order has no justification as a contempt proceeding. And, as it has no purpose except to force by imprisonment the payment of money on debts, it is difficult to see why it is not aptly called imprisonment for debt. When the imprisonment occurs under such circumstances, no matter what may be said to the contrary, it remains a fact that the debtor is arrested and imprisoned to force the payment of a debt in whole or in part." (Concurring opinion per Shelby, C. J.) Quoted on other points at §§ 1643, 1845.

§ 1842. Clear, Certain, Convincing or Satisfactory Proof, or Proof beyond Reasonable Doubt, Requisite.—The evidence must, therefore, show with certainty and to the satisfaction of the court, and, perhaps, even beyond a reasonable doubt, that the bankrupt or other person proceeded against does still possess the means of complying with the order. Thus, the proof must at least be satisfying and certain.⁵⁷

Compare, analogously, similar rule as to punishment for contempt for failure to obey order, *In re Levy & Co.*, 15 A. B. R. 169, 142 Fed. 442 (C. C. A.): "We are not unmindful of the general rule that the power to imprison for contempt in such cases should be exercised with great caution and only upon proof which establishes the facts found beyond a reasonable doubt, or which must, in any event, be clear and convincing. But we are satisfied that upon the facts herein a jury would necessarily find the fact of possession or control upon an admitted receipt of goods and repeated refusals to explain or account for their disappearance. The question of the power and duty of the court in such cases has been so often passed upon that it is unnecessary to discuss it in this connection."

Samel v. Dodd, 16 A. B. R. 167, 142 Fed. 68 (C. C. A. Ga.): "In such cases the order to deliver should be based upon clear and convincing proof that the party charged has possession and control of the property, since the penalty of disobedience is imprisonment for contempt. The order operates in personam.

⁵⁷ *In re Purvine*, 2 A. B. R. 787, 96 Fed. 192 (C. C. A. Tex.); *In re Alphin & Lake Cotton Co.*, 12 A. B. R. 653, 131 Fed. 824 (D. C. Ark.); *quære*, *Scheer v. Brown*, 12 A. B. R. 178, 130 Fed. 328 (C. C. A. Ark., affirmed by Sup. Ct., 12 A. B. R. 674, 195 U. S. 171); *In re DeGottardi*, 7 A. B. R. 723, 114 Fed. 328 (D. C. Calif.); *In re Gilroy & Bloomfield*, 14 A. B. R. 627, 140 Fed. 733 (D. C. N. Y.), [1867] *In re Salkey*, 21 Fed. Cases, No. 12,253, 11 N. B. Reg. 423; *In re Lesaius*, 21 A. B. R. 23, 163 Fed. 614 (D. C. Pa.); instance held proof insufficient, *In re*

(Wolfe) *Adler*, 21 A. B. R. 371, 170 Fed. 634 (D. C. Okla.); instance, *In re Baum*, 22 A. B. R. 295, 169 Fed. 410 (C. C. A. Ark.); *In re Greer*, 26 A. B. R. 811, 189 Fed. 511 (D. C. Ark.); *In re Haring*, 27 A. B. R. 285, 193 Fed. 168 (D. C. Mich.). To same effect, *In re Sax*, 15 A. B. R. 455 (D. C. Penn.).

Compare, *In re Taylor*, 7 A. B. R. 410 (D. C. Colo.), where the court says "a bankrupt cannot be imprisoned indefinitely" (should not be imprisoned at all) "when it is not certainly known that he has the money he is called upon to surrender."

upon the person of the offender, by requiring him to do the thing commanded upon pain of punishment for refusal; and such an order is erroneous, as matter of law, unless it plainly and affirmatively appear from the record that he has the power to comply with its requirements. If, having the property, he fail to surrender it in obedience to the order of the court, he voluntarily submits himself to the consequences."

Indeed, the almost overwhelming number of the decisions have laid down the rule (although not in cases where the distinction has been sought to be made, and in many instances in cases of contempt rather than of summary orders to surrender assets) that the court must be satisfied "beyond a reasonable doubt" upon this point or that the evidence must be "practically incontestible."⁵⁸

Boyd v. Glucklich, 8 A. B. R. 393, 116 Fed. 131 (C. C. A. Iowa): "And it must be made to appear by evidence which leaves no reasonable doubt in the mind of the court on the subject. Evidence which is merely persuasive will not suffice."

In re Feldser, 14 A. B. R. 216, 134 Fed. 307 (D. C. Pa.): "It is necessary that it should be, as stated by the referee, found beyond a reasonable doubt that the person against whom the order is made has the funds or property in his possession or control."

In re Walder, 16 A. B. R. 41 (D. C. Conn.): "If the order shall be affirmed, and the bankrupt shall fail to comply with its terms, contempt proceedings will naturally follow, and no good purpose would be served by adopting a lower order of proof now than will be required when action shall be taken in the next step."

Ripon Knitting Works v. Schreiber, 4 A. B. R. 299, 101 Fed. 810 (D. C. Wash., affirmed, on review, in 104 Fed. 1006): "His answer is not conclusive, but the rule in such cases requires that the denial be overcome by evidence proving beyond a reasonable doubt that the bankrupt actually has the present possession or control of money, or that any alleged transfer or other disposition of it is a mere subterfuge which does not prevent him from producing it."

In re Adler, 12 A. B. R. 19, 129 Fed. 502 (D. C. Tenn.): "The court has no doubt of the power of the court, where it reasonably appears that the bankrupt has the money in his possession or under his control, to compel him to pay it over; but that fact must appear by something more substantial than mere presumptions or inferences taken from such circumstances as those which have been proven in this case. To invoke that power requires something like incontestible proof as against the bankrupt's denial that he has the money. The fact that he accounts falsely for his dissipation of the money, the fact that he does not satisfactorily disclose his uses of it, the fact that he evades the exhibition of his conduct in the premises, may indicate that he has defrauded his creditors, that he has dealt falsely with them, that he has egregiously perjured himself and sworn the truth, and may invoke other remedies under the statute; but not this of a peremptory order to pay the money to the trustee, and punishment by contempt for a failure to do so. That remedy applies only

⁵⁸. *In re Rosser*, 4 A. B. R. 153, 101 Fed. 562 (C. C. A. Mo.); inferentially, *In re Leinweber*, 12 A. B. R. 175 (D. C. Conn.); *In re Anderson*, 4 A. B. R. 640, 103 Fed. 854 (D. C., reversed, on other grounds, in *McGahan v. Anderson*, 7 A. B. R. 64, 113 Fed. 115); *In re Friedman*, 2 A. B. R. 301 (Ref. N. Y.); *Trust Co. v. Wallis*, 11 A. B. R. 360, 126 Fed. 464 (C. C. A. Penn.). Com-

pare same rule, contempt proceedings for failure to surrender assets, *In re Switzer*, 15 A. B. R. 470 (D. C. S. C.).

In re Berman, 21 A. B. R. 139, 165 Fed. 383 (D. C. Pa.); *In re Mize*, 22 A. B. R. 577, 172 Fed. 945 (D. C. Ala.); *Stuart v. Reynolds*, 29 A. B. R. 412, 204 Fed. 709 (C. C. A. Ala.), quoted at §§ 1841, 1843, 1845.

to a fund which can be designated and traced into his possession, so that it is, in a legal sense, a tangible fund on which the court can lay its hands; and it cannot be made to apply to some intangible money supposed to be kept in his possession which he can be forced to pay by raising or procuring the money to meet the orders of the court. No doubt many bankrupts could be made, under the coercion of imprisonment, to find the money with which to meet such a demand; but the law does not proceed upon the theory of thus compelling a bankrupt to pay his creditors that which he owes them. It would be in substance and in fact a mere revival of the discarded remedy of imprisonment for debt. Therefore, unless the court can see that the bankrupt is in possession of the money, and withholding it wrongfully, it will not make such an order as that which is applied for in this case. The bankrupt may be indicted under the criminal features of the act, his discharge may be refused, he may be compelled by contempt proceedings to answer questions which he evades and refuses to answer, and to disclose the rights of action that may belong to the trustee by reason of his dealings with others; and thus in many ways he may be compelled to give the fullest statement of his affairs; but, no matter how fraudulent his conduct may be, the creditors cannot resort to this method of compelling him to pay his debts, when there is not sufficient proof that he is concealing money or other property in actual possession or control."

In *re Goldfarb Bros.*, 12 A. B. R. 389, 131 Fed. 643 (D. C. Ga.): "The evidence in such a proceeding should satisfy the court beyond a reasonable doubt that the bankrupt has the money or goods in his possession and control, and is able to turn them over when so ordered. * * *

"While the evidence in the case at bar showed very strong probability, and even more than a probability, that the bankrupts in this case have not dealt fairly with their creditors or with the trustee, it is not, to my mind, sufficiently definite and convincing to justify me in saying from this evidence that they are withholding any definite amount, or anything like an approximate amount of money or goods from the trustee. Certainly it fails to show with any degree of satisfaction, that they have withheld the amount found by the referee as in their hands. If there was evidence in the record to show with some definiteness the amount of stock on hand in the bankrupts' stores on the first of June, 1903, and any evidence to show the amount of goods sold by them for cash which they did not deposit in bank; how much of this money was paid out, or if not paid out, with some degree of certainty, how much was retained, data would then be had from which to make some fair calculation. But in the absence of this, I do not think that any one can take this evidence, and this entire record, and say that the bankrupts have any amount of goods or money, fixing it even approximately, in their hands, which has not been turned over to the trustee."

In *re Mayer*, 3 A. B. R. 533, 98 Fed. 839 (D. C. Wis.): "An order requiring the bankrupt to turn over money or property withheld from the trustee, when the bankrupt denies possession or control, can be so enforced only on indubitable testimony which establishes either the fact of his present possession, or that a purported transfer or disposition is a mere subterfuge, by which the property manifestly remains within his control, and can be produced by him. And in a proceeding of this nature the order is sustainable only to the extent the testimony so establishes the fact of actual possession or control with all reasonable doubt resolved in favor of the bankrupt."

The better rule on reason would seem to be that the proof need not be beyond a reasonable doubt; that, because imprisonment for contempt may

be the punishment for failure to comply with the order, does not make the proceedings criminal, and the rules of evidence of criminal cases do not apply.⁵⁹

In *re Cole*, 16 A. B. R. 303, 144 Fed. 392 (C. C. A. Me.): "The issue whether an order should run against a bankrupt, requiring the bankrupt to make payment to the trustee, is purely of a civil character: and therefore that part of the order before us which directed payment may be supported by a mere preponderance of the evidence, presumptions or inferences."

In *re Alphin & Lake Cotton Co.*, 14 A. B. R. 197, 134 Fed. 477 (D. C. Ark.): "On behalf of the respondent it is urged that, to warrant a finding against respondent, the evidence must be beyond a reasonable doubt; that in view of the fact that, if an order is made requiring the respondent to pay over money, and he fails to comply with it, he will be imprisoned for contempt of court, it is urged that the proceedings must be treated as a criminal proceeding, and be governed by the same rules. This court cannot assent to this proposition. If the fact that a failure to comply with the order of the court may result in imprisonment of the respondent for contempt makes it a criminal case, many proceedings, and especially proceedings in courts of equity, would have to be treated as criminal proceedings. The failure on the part of a defendant to execute a conveyance decreed by a court of equity in a proceeding for specific performance may be enforced by imprisonment as for contempt. Refusal to answer interrogatories in a bill of discovery, refusal to pay alimony in a divorce suit, disobedience to a writ of mandamus, or violation of an injunction may result in such punishment; but no one will contend that for this reason such proceedings are in the nature of criminal actions. The punishment for contempt in bankruptcy proceedings is simply for disobedience of the judgment of the court after it is found that the respondent has money or property belonging to the bankrupt estate in his possession or under his control, and, although able to comply with the order of the court, willfully refuses to do so. These provisions in the Bankruptcy Act, authorizing courts of bankruptcy to enforce obedience to their orders by punishment as for contempt are neither novel nor unusual. They were included in every Bankruptcy Act, and similar provisions have been enacted by almost every State in the Union, including the State of Arkansas. In proceedings supplemental to or in aid of executions, courts are authorized by these statutes to enforce the surrender of assets subject to execution, and for this purpose may commit to jail any person refusing to comply with such order. In this State, section 3312, Kirby's Dig. St. Ark., contains such a provision. And by sections 61 and 62, Kirby's Dig., probate courts are authorized to enforce their orders for the surrender of property belonging to the estate of a deceased person by attachment. These statutes have been uniformly sustained as civil proceedings."

In *re Dickens*, 23 A. B. R. 660, 175 Fed. 808 (D. C. Ala.): "The authorities are agreed that a bankrupt should not be committed for contempt for failing to obey an order requiring him to turn over money or property to his trustee, unless the court is satisfied beyond a reasonable doubt of his present ability to comply with the order."

In *re Cramer*, 23 A. B. R. 637, 175 Fed. 879 (D. C. Mass.): "A consideration of the facts set forth by the referee in his report and of the evidence which

⁵⁹. Compare, to similar effect, *Moody v. Cole*, 17 A. B. R. 818 (D. C. Me.). But compare, *In re Walder*, 16 A. B. R. 42 (D. C. Conn.), quoted *supra*, § 1842. And compare, *In re Lasch*, 12 A. B. R. 158 (D. C. Penn.), where it is held to be "in the nature of a criminal proceeding."

accompanies the report has led me to believe that the referee must have acted, in refusing the order asked for, upon the theory that proof beyond a reasonable doubt was necessary to sustain a finding that there had been any concealment of property from the trustee. But that a fair preponderance of evidence in favor of such a conclusion is enough seems to me sufficiently well settled, at least in this Circuit. In *re Cole* (C. C. A.), 16 Am. B. R. 302, 144 Fed. 392. * * * That there was such a preponderance of evidence in this case I find myself unable to doubt."

However, the court should not make the order unless, on the same evidence, if the order be disobeyed, the court would punish for contempt.⁶⁰

Impliedly, In *re (Wolfe) Adler*, 21 A. B. R. 371, 170 Fed. 634 (D. C. Okla.): "Ordinarily in cases of this character where the bankrupt conceives the order of the referee to be invalid, he refuses to obey the order, whereupon the referee certifies the facts to the judge, for a summary hearing, and punishment as for contempt, if he finds the fact warrants it. While this case comes up on petition of the bankrupt to review the order of the referee, it practically raises the questions which would come up on a citation for contempt, for the reason that unless the order is one the enforcement of which can properly be effected by imprisonment for contempt, it would be a futile order to make, and the case will therefore be treated as one in which an order has been disobeyed and is before this court in a contempt proceeding. * * * If I am correct in the conclusion that the evidence upon which this order is based is not sufficient to warrant this court to order the bankrupt imprisoned for contempt, should he fail to obey it, then it follows that the order should not have been made. An order which cannot be enforced is a dead letter. The order will therefore be annulled and set aside."

Nor should the order be made upon a third person where there exists a commingling of the property belonging to the bankrupt estate with other property, unless the property belonging to the estate can be followed and sufficiently identified to enable a court officer to take it into his possession.

In *re Jackier*, 24 A. B. R. 790, 179 Fed. 720 (D. C. Pa.): "It is clear that such an order should not be made unless the goods can be followed and sufficiently identified to enable the marshal to take them into his possession. The evidence in the present case does not go far enough to meet these requirements, and for this reason the petition must fail. In a plenary suit where a receiver or a trustee may recover a verdict for the value of goods even if the goods themselves cannot be precisely identified, a recovery may rest upon proof of a somewhat less definite quality, but in a proceeding like this it is necessary to follow specific articles with reasonable certainty."

60. In *re Walder*, 16 A. B. R. 42 (D. C. Conn.), quoted *supra*, this paragraph. In *re Ogles*, 2 A. B. R. 514 (Ref. Tenn.).

But compare, inferentially *contra*, In *re Hausman*, 10 A. B. R. 64, 121 Fed. 984 (C. C. A. N. Y.), where the inference is given that the matter of present possession may be relitigated upon the contempt proceedings.

Compare, also, In *re Mayer*, 3 A. B. R. 534, 98 Fed. 839 (D. C. N. Y.).

But that the proceedings for order of surrender differ in character from those for contempt, see In *re Davison*, 16 A. B. R. 338, 143 Fed. 673 (D. C. R. I.); In *re Cole*, 16 A. B. R. 303, 144 Fed. 392 (C. C. A. Me.).

§ 1843. Bankrupt's Sworn Denial Not Conclusive.—The bankrupt's⁶¹ or agent's⁶² sworn denial is not conclusive.

In *re Meier*, 25 A. B. R. 272, 182 Fed. 799 (C. C. A. Mo.), quoted post, § 1850: "The settled rule is that, when property of a bankrupt estate is traced to the possession of one who receives it upon the eve of the bankruptcy of its owner, it is presumed to remain in his possession or under his control until he satisfactorily accounts to the court of bankruptcy for its disposition or disappearance; that the burden is upon him to satisfactorily so account for it; and that he cannot escape an order for its surrender by simply denying under oath that he has it, or that it is the property of the bankrupt estate."

In *re Weber Co.*, 29 A. B. R. 217, 200 Fed. 404 (C. C. A. N. Y.): "Upon the application to punish for contempt he made no explanation as to how or why it was that this particular sum had disappeared, merely denying that he ever had it. His statement that he had no money, when the proceeding for contempt was instituted, without some such explanation was insufficient and the judge quite properly held him on contempt for not paying it over. To excuse disobedience of the order by such general denial would make it easy to evade the requirements of the Bankruptcy Act."

Obiter, In *re Goldfarb*, 12 A. B. R. 386, 131 Fed. 643 (D. C. Ga.): "It will not do, of course, to say that the mere denial of the bankrupt that he has any money or effects in his possession should be sufficient to exonerate him from a charge of this kind."

In *re Schachter*, 9 A. B. R. 497 (D. C. Ga.): "Otherwise the court would be powerless, in the face of the bankrupt's oath, to require the production of property, however conclusive might be the evidence that such property was in his possession or control."

In *re Friedman*, 18 A. B. R. 712, 153 Fed. 939 (D. C. N. Y., affirmed in 20 A. B. R. 37, 161 Fed. 260, C. C. A.): "But if any person into whose possession money is traced can avoid the legitimate consequence of the possession of that money by swearing that he no longer has it, or never had it, the administration of justice would become a farce."

In *re Marks*, 23 A. B. R. 911, 176 Fed. 1018 (D. C. Pa.): "Certainly, his bare denial of present ability to pay may be properly regarded with suspicion, and he may be required to satisfy the court with clearness that obedience to the order is wholly beyond his power. Such situations must be dealt with as they arise; no general rule can be laid down, and each case must stand upon its own facts."

61. In *re Schlesinger*, 3 A. B. R. 342, 97 Fed. 930 (D. C. N. Y., on review, 4 A. B. R. 361, 102 Fed. 117); In *re McCormick*, 3 A. B. R. 340, 97 Fed. 566 (D. C. N. Y.); *Schweer v. Brown*, 12 A. B. R. 178, 130 Fed. 328 (C. C. A. Ark., affirmed in 12 A. B. R. 673, 195 U. S. 171); *Ripon Knitting Works v. Schreiber*, 4 A. B. R. 299, 101 Fed. 810 (D. C. Wash.); [1867] In *re Salkey*, 21 Fed. Cases, No. 12,263; In *re Gerstel*, 10 A. B. R. 411, 123 Fed. 166 (D. C. Ills.); In *re Kane*, 12 A. B. R. 445, 131 Fed. 386 (D. C. N. Y.); In *re Rosser*, 2 A. B. R. 746, 96 Fed. 192 (D. C. Mo., on review, 4 A. B. R. 153, 101 Fed. 562, C. C. A. Mo.); In *re Purvine*, 2 A. B. R. 787, 96 Fed. 192 (C. C. A.

Tex.); In *re Epstein*, 15 A. B. R. 711 (D. C. Penn.); analogously (contempt), obiter, *Moody v. Cole*, 17 A. B. R. 818 (D. C. Me.); analogously (contempt), In *re Lasky*, 20 A. B. R. 729, 163 Fed. 99 (D. C. Ala.); In *re Meier*, 25 A. B. R. 272, 182 Fed. 799 (C. C. A. Mo.); In *re Goodman*, 27 A. B. R. 697, 196 Fed. 566 (D. C. Ohio); *Kirsner v. Taliaferro*, 29 A. B. R. 832, 202 Fed. 51 (C. C. A. Va.); In *re Lippman*, 25 A. B. R. 874, 184 Fed. 551 (D. C. N. Y.); instance, In *re Belluscio*, 25 A. B. R. 660 (Ref. N. Y.).

62. In *re Famous Clothing Co.*, 24 A. B. R. 780, 179 Fed. 1015 (D. C. N. Y.).

It has been held, however, that a denial by the bankrupt may be conclusive in some cases.

Stuart v. Reynolds, 29 A. B. R. 412, 204 Fed. 709 (C. C. A. Ala.): "The argument claims, in effect, that the trial judge should give no weight to the contemnor's sworn denial. Reynolds, by sworn answer, denied the charges against him. The answer of the contemnor is not taken as true, in the sense that it cannot be contradicted. It has been held by English common law writers as unassailable, and some federal courts have followed that rule. *Rapalje on Contempt*, § 119, and cases cited. The cases on both sides of the proposition are too numerous for citation, but they may be found collected in the briefs and opinion in *United States v. Shipp*, 203 U. S. 563, where the court decides that 'when the acts alleged consist in taking part in a murder it cannot be admitted that a general denial and affidavit should dispose of the case;' but the opinion recognizes the fact that there may be cases in which the answer would be conclusive. 'It may be that even now,' said the court, 'If the sole question were the intent of an ambiguous act, the proposition would apply.' In cases, like the present case, where the bankrupt is accused of withholding and refusing to surrender large stocks of goods, and he answers on oath, denying possession and control of them, his control and possession being an affirmative allegation of the trustee, it is not at all unreasonable to look on his answer as sufficient to secure his discharge, unless evidence of the most convincing kind is offered to sustain the charge against him. The affirmative in such case would not be difficult to prove if the charge were true. In cases where it is charged that he withholds large sums of money, and he makes sworn denial, it is not consistent with the admitted rule that his guilt, to authorize commitment, must be proved to the exclusion of reasonable doubt—to say that the burden can be put on the contemnor to prove his negative averment.

"In such cases, the rule undoubtedly goes to this extent, to quote the words of an author, which he sustains by many citations of authority." Quoted on other points at §§ 1841, 1845.

§ 1844. But Almost Incontestible Evidence Requisite to Overcome It.—But, at any rate, it requires something like incontestible evidence, or evidence beyond a reasonable doubt, to overcome the denial.⁶³

Trust Co. v. Wallis, 11 A. B. R. 360, 126 Fed. 464 (C. C. A. Pa.): "If the bankrupt denies that he has possession or control of the property, or, if a third person in possession thereof claims to hold it, not as the agent or representative of the bankrupt, but by title adverse to him, and there is no evidence to indisputably show that such denial or claim is false or fraudulent, and that the case is one of simple concealment or refusal on the part of the bankrupt, or

⁶³. In *re Ripon Knitting Wks. v. Schreiber*, 4 A. B. R. 299, 101 Fed. 810 (D. C. Wash.); In *re Friedman*, 2 A. B. R. 301 (Ref. N. Y.); In *re Mayer*, 3 A. B. R. 533, 98 Fed. 839 (D. C. Wis.); inferentially, In *re Gilroy & Bloomfield*, 14 A. B. R. 627, 140 Fed. 733 (D. C. N. Y.); analogously (contempt for failure to obey order), *Moody v. Cole*, 17 A. B. R. 818 (D. C. Me.). But compare, inferentially contra, In *re Lasky*, 20 A. B. R. 729, 163 Fed. 99 (D. C. Ala.), quoted at § 1850; instance where

evidence found insufficient, In *re (Wolfe) Alder*, 21 A. B. R. 371, 170 Fed. 634 (D. C. Okla.); impliedly, In *re Dickens*, 23 A. B. R. 660, 175 Fed. 808 (D. C. Ala.), quoted at §§ 1840, 1842, 1845; *Stuart v. Reynolds*, 29 A. B. R. 412, 204 Fed. 709 (C. C. A. Ala.), quoted at §§ 1841, 1843, 1845; In *re Haring*, 29 A. B. R. 387, 193 Fed. 168 (C. C. A. Mich.); instance, In *re Chamelin*, 25 A. B. R. 570, 184 Fed. 553 (D. C. Pa.).

the one in possession, to deliver up the property as ordered, it would be an unwarranted stretch of power on the part of the court to resort to summary proceeding for contempt for the enforcement of its order."

Samel v. Dodd, 16 A. B. R. 170, 142 Fed. 68 (C. C. A. Ga., concurring opinion): "It follows unquestionably that an order imprisoning a bankrupt for contempt for failure to obey a decree to pay money or surrender goods into court is erroneous as matter of law, where the bankrupt by sworn answer denies that he has the money or the goods, and it does not appear clearly and affirmatively from the record, notwithstanding his denials, that he has the power to comply with the decree. The bankrupt is at least entitled to that much protection, if, indeed, the courts are to refuse to follow the wise rule of the common law which makes the sworn denials of the answer sufficient defense to the contempt proceedings, leaving the question of the truth of the answer to be contested in a prosecution for perjury. * * *

"The bankrupts, in their answers, have sworn that they have not in their possession or under their control the money or goods involved in this proceeding. It seems to me that any evidence that conclusively showed they presently had in possession and control either the money or the goods would necessarily show where the same was kept or deposited, so that it could be reached by the process of the bankruptcy court, or of some court in a suit by the trustee. But however that may be, the record in this cause, taken as a whole, fails to show that the bankrupts had in their possession at the date of the order committing them for contempt either the money or the goods referred to. If the bankrupts have sworn falsely in their pleadings or on their examination—and this proceeding is based solely on that hypothesis—the law provides for their punishment on indictment and conviction by a procedure which secures to them the right of trial by jury with all its constitutional safeguards."

In re Adler, 12 A. B. R. 19, 129 Fed. 502 (D. C. Tenn.): "To invoke that power requires something like incontestible proof as against the bankrupt's sworn denial that he has the money."

§ 1845. Proof of Present Possession or Control Requisite.—Present possession or control must be proved. It will not do simply to prove the bankrupt ought still to have the possession or control: it must be proved that he actually still has possession or control.⁶⁴

⁶⁴ *Boyd v. Glücklich*, 8 A. B. R. 393, 116 Fed. 131 (C. C. A. Iowa); impliedly, *In re Adler*, 12 A. B. R. 19, 129 Fed. 502 (D. C. Tenn.); *In re Ogles*, 2 A. B. R. 514 (Ref. Tenn.).

But compare, *In re Wilson*, 8 A. B. R. 612, 116 Fed. 419 (D. C. Ark.), and *In re Tudor*, 4 A. B. R. 78, 100 Fed. 796 (D. C. Colo.), where the courts seemed to think it proper to "allow" only for "legitimate" expenses in making the computation necessary to deduce present possession of assets. See, also, cases cited in these opinions.

Analogously (contempt proceedings), *In re Davidson*, 16 A. B. R. 337, 143 Fed. 173 (D. C. R. I.).

Long Delay Fatal.—Long delay in filing the petition for surrender may be fatal to the trustee's claim. Thus,

where discharge was refused on the ground of concealment of assets, a delay of four years in filing a petition to surrender the assets will nullify the effect as *res judicata* of the refusal of the discharge. *In re Barton Bros.*, 18 A. B. R. 98, 149 Fed. 620 (D. C. Ark.).

Refusal of Discharge as Res Judicata.—As to the effect of a refusal of discharge on the ground of concealment of assets, see: *In re Barton Bros.*, 18 A. B. R. 98, 149 Fed. 620 (D. C. Ark.): "It is *res adjudicata* that these bankrupts did not surrender all of their estate, and that their schedules were false, but there is a wide difference between denying a bankrupt his discharge on the ground that his schedules are false, and making an order four years after his bankruptcy com-

[On review of contempt order rather than of order to surrender assets.] *Stuart v. Reynolds*, 29 A. B. R. 412, 204 Fed. 709 (C. C. A. Ala.): "But the counsel seek also to apply a rule that is in fact applicable to a class of criminal cases—that 'the recent possession of stolen property casts upon the possessor a suspicion of guilt from which he should free himself.' The argument, in effect, is, that, the recent unexplained possession of stolen goods would be sufficient to adjudge the possessor guilty of larceny, unless he rebutted the inference; and that, therefore, by 'analogy,' the recent possession of the goods by the bankrupt is sufficient, unexplained, to show that he still has them, and therefore sufficient to prove, as required by law, that he is in contempt in failing to produce them. But the possession of stolen property, however recent and unexplained, creates no presumption of law that the possessor committed the larceny, and instructions to that effect, 'casting the burden of proving the innocent character of the possession upon the accused,' is erroneous. Underhill on Criminal Evidence (2d edition), § 299, and cases there cited. Such possession, in connection with proof of the larceny is, of course, legal evidence from which the jury may infer guilt. But there is no analogy between the larceny case and the contempt case. The possession in the former case is evidence against the possessor only when the corpus delicti is proved. The inference against him is based on the fact that the property has been proved to have been stolen, and such possession, though it does not change the burden of proof, casts suspicion on the possessor. But the property that the respondent is charged with withholding has not been stolen. His possession is assumed to have been acquired so as to vest title in him. His former possession of it casts no suspicion on him. There is no analogy between the instant case and larceny case that relieves the trustee from proving affirmatively and as required by law that the respondent had in his possession the property in question, and was therefore able to obey the referee's order. The fact that the property passed into the possession of the bankrupt is, of course, one step in the effort to prove that he still has it. But if the property consists of twenty thousand dollars' worth of 'goods, wares and merchandise,' as indicated in one of the alternative recitals of the referee's order, this proceeding, of itself, is sufficient to show that he has not in his actual possession goods of such bulk and value, for if he so held them, they would be taken from him by writ. If, when the referee's report and finding says that the property withheld is 'goods, wares, merchandise, money, and other property,' it is meant that the goods, etc., shown by the 'expert's' examination of his books, have been sold, and that he has in money the \$20,000, then, of course, to show guilt proof is required that he has in present possession the \$20,000 in money. No case is made for the application of the doctrine of 'presumptions' so as to dispense with the necessity for evidence."

Amer. Trust Co v. Wallis, 11 A. B. R. 360, 126 Fed. 464 (C. C. A. Penn.): "Has the referee, or the court in bankruptcy, power to order the bankrupt to deliver and turn over to the trustee in bankruptcy, money collected from his debt-

selling him to pay over the proceeds illegally withheld from his trustee."

See, in addition, *In re Ruos* (No. 2), 21 A. B. R. 257, 164 Fed. 749 (D. C. Pa.); impliedly, *In re (Wolfe) Alder*, 21 A. B. R. 371, 170 Fed. 634 (D. C. Okla.); *In re Mize*, 22 A. B. R. 577, 172 Fed. 945 (D. C. Ala.); impliedly, *In re Berman*, 21 A. B. R. 139, 165 Fed. 383 (D. C. Pa.); *In re Holland*, 23 A. B. R. 835, 176 Fed. 624 (D. C. N. Y.), quoted at §§ 1833, 1840; analogously,

in contempt proceedings, *In re Marks*, 23 A. B. R. 911, 176 Fed. 1018 (D. C. Pa.), quoted at § 1857; obiter, *In re Soloway & Katz*, 28 A. B. R. 225, 196 Fed. 132 (D. C. Conn.); *In re Reynolds*, 27 A. B. R. 200, 190 Fed. 967 (D. C. Ala.); *In re Haring*, 27 A. B. R. 285, 193 Fed. 168 (D. C. Mich.); *In re Frank*, 25 A. B. R. 486, 182 Fed. 794 (C. C. A. N. D.); instance, *In re Jablin*, 28 A. B. R. 54, 194 Fed. 228 (D. C. N. Y.).

ors after he had received notice or knowledge of the filing of the petition by creditors to have him adjudged a bankrupt, which money has since passed into the possession of others and is not under the control of the bankrupt? * * * In the absence of fraud or concealment, the bankrupt court can only order the delivery of property to the trustee which the bankrupt is physically able to deliver up, having the same in his possession or control. If it shall appear that he is not physically able to deliver the property required by the order, then, confessedly, proceedings for contempt, by fine and imprisonment, would result in nothing, certainly not in compliance with the order. The contempt in this case could only be purged by a reiteration of the physical impossibility to comply with the order whose disobedience is being thus punished. An order made under such circumstances would be as absurd as it is inconsistent with the principles of individual liberty. But it may be said that, to have collected this money from his debtors and distributed it to his creditors, with knowledge of the filing of the petition in bankruptcy, was in contempt of the Bankrupt Law and of the proceedings in bankruptcy, which were a caveat to all the world as to the effect of such proceedings upon the property of the bankrupt in case he should be so declared. This, however, would be but a constructive contempt, and not liable to the summary punishment by fine and imprisonment which may be inflicted for actual contempt, committed in the presence of the court or by open and defiant refusal to comply with its lawful commands, where compliance is physically possible."

Samel v. Dodd, 16 A. B. R. 169, 142 Fed. 68 (C. C. A. Ga., concurring opinion): "But, unless the person can perform the act commanded, the court has no authority to punish for a failure to perform it. Any other rule would be unreasonable and unjust. To imprison one for not doing what he cannot do is inconsistent with the principles of individual liberty. There is no statute or law which confers such authority. Imprisonment under such circumstances for failure to pay money may force the friends of the prisoner to raise and pay the required sum, but such imprisonment is unwarranted by law in a jurisdiction where imprisonment for debt is forbidden. Where the prisoner has the power to comply with the order, having the money or thing in question in his possession, he may, of course, be punished for his failure to surrender it, without conflict with any rule of law against imprisonment for debt."

In re Baum, 22 A. B. R. 295, 169 Fed. 410 (C. C. A. Ark.): "The court, of course, could not require the petitioner to do an impossible thing and then punish him for refusing to perform it. Therefore, from the fact that the court ordered him to pay over the money, it must necessarily have had before it testimony sufficient to satisfy it of his ability to comply."

Impliedly (on contempt for failure to surrender), *In re Rogowski*, 21 A. B. R. 553, 166 Fed. 165 (D. C. Ga.): "If the rule be adopted, announced in some cases, that where a bankrupt shortly before his failure has on hand a large stock of merchandise, and when proceedings in bankruptcy are instituted he is found to have but a small amount of goods, the stock being depleted to such an extent that it could not have occurred in the ordinary course of business, and there are circumstances to indicate that the goods have been purposely and fraudulent removed so as to prevent their going into the hands of the trustee in bankruptcy, that then the court may require the bankrupt to produce the goods or give some reasonable explanation of their disappearance, and on his failure so to do may hold him for contempt, then a case is made out by the record here. * * * On the other hand, if the rule be that, notwithstanding such condition of things as indicated above, the receiver, trustee, or creditor proceeding against the bankrupt is unable to point out any particular property or cash so re-

moved, and its location, definitely and specifically, contempt proceedings are not justified, then no case is made here. I think the latter rule has been adopted by the Circuit Court of Appeals for this Circuit in *Samel v. Dodd*."

In re *Walder*, 16 A. B. R. 42 (D. C. Conn.): "The real question, then, is whether or not the bankrupt has accounted for the disappearance of the goods which he has been ordered to return, or, to put it more definitely, whether his explanation leaves the matter in such a shape that the court can find beyond a reasonable doubt that he now has possession or control of the goods, or of the money into which they have been converted."

In re *Barton Bros.*, 18 A. B. R. 100, 149 Fed. 620 (D. C. Ark.): "It is seen by an examination of the two decisions last quoted, unless they were in possession of the money at the time the order is made to pay over, the court has no power to make the order. If the court were to make the order for them to pay over when they were without the means of paying over, the court would then be requiring them to do an impossible thing, and the effect of such an order would be equivalent to imprisonment for debt."

In re *Goldfarb*, 12 A. B. R. 389, 131 Fed. 643 (D. C. Ga.): "A bankrupt cannot be required, under a proceeding for contempt, to do that which it is out of his power to do. The evidence in such a proceeding should satisfy the court beyond a reasonable doubt that the bankrupt has the money or goods in his possession and control and is able to turn them over when so ordered. If he has placed them out of his possession and control, no matter how foolishly or how wrongfully, he cannot be required by order to turn them over to a receiver or to a trustee."

In re *Mayer*, 3 A. B. R. 534, 98 Fed. 839 (D. C. Wis.): "It is not applicable, however, to reach property beyond the present control of the bankrupt, and in the hands of third parties claiming title derived prior to the proceedings in bankruptcy, although the transaction is manifestly fraudulent. Nor can this means or provision be employed to punish for frauds committed by the bankrupt against the Bankrupt Act, nor can it be used to coerce the bankrupt or transferees to make restitution of money or property previously transferred in fraud of the act. Frauds which are made criminal by the act are punishable only on conviction by the verdict of a jury, or on plea of guilty, and fraudulent transfers which have been consummated cannot be reached by this summary proceedings. * * *

"The finding of merchandise to the amount and value of \$20,392.39 in the hands of the bankrupt is predicated on a showing which raises strong suspicion of a large amount of goods unaccounted for during the half year preceding the failure, but the testimony is deemed insufficient to establish beyond reasonable doubt the fact of abstraction of goods from the stock. No surreptitious transactions are shown respecting the goods, notwithstanding inquiry and search to that end, which appear to have been diligently pursued. The discrepancy stated in the findings rests upon valuations taken of the stock on hand without the presence of the bankrupt, not in reference to the present inquiry, not based on the bills rendered for the purchases nor on the actual cost to the bankrupt, and offered for this issue after the goods have passed beyond reach for testing the valuation by the bills—a test which would otherwise be practicable for a large portion of the stock made up of recent purchases. The testimony of certain of the appraisers that such valuations would approximate the cost to the bankrupt is forcibly met by proof of numerous instances wherein the cost, as shown by the bills, materially exceed the appraisal; and, after extended enumerations from the inventory in comparison with the bills, an estimate of such excess is tendered which would cover the discrepancy. Whether the shortage is thus satisfactorily

accounted for is not the test, but it is sufficient that the valuation which constitutes the sole basis of the charge is placed in doubt, both as to the definite amount and to the fact of the surreptitious taking of goods, and no ground is established for an order of this nature to turn over either certain goods or a definite amount on pain of imprisonment; and, so regarded, the order, to that extent, is not sustainable."

In re Milk Co., 16 A. B. R. 731 (D. C. Pa.): "It is now sought to make him personally answerable for this money; not by suit, upon the ground that it was unwarrantably paid out, with the ordinary incidents of execution, etc., in case a judgment should be recovered; but by summary order of court, for disobedience of which he may be attached and committed, for contempt. It is not pretended that the money sought to be reached is actually in his possession, or control, nor is any concealment or subterfuge alleged, or if it is, it has not been made out. All that is contended for is, that it shall be treated as constructively in his hands; that is to say, that he shall be held, as though it were, because it ought to be. But this is a misconception of the remedy invoked, and the power of the court under it. It is effective to lay hold of a specific fund or thing, under the dominion or control of the party ruled, but cannot legitimately go beyond that. Undoubtedly the court will not permit a colorable evasion, and that which is held by another, in his interest, or with his connivance, is the same as though held by the party himself. *Mueller v. Nugent*, 184 U. S. 1, 7 Am. B. R. 224. An adverse claim on the other hand made in good faith on what is apparently a sufficient basis, will be respected, and, subject always to the right to determine whether it is so made, the court will not undertake to override or pass upon it. It is true that there are cases where a party has been required to disgorge funds which are traced into his hands, notwithstanding his protest that he has spent them in payment of debts, or has otherwise disposed of them. In re Gerstel, 10 Am. B. R. 411; In re Michael Kane, *Ib.* 478; *Schweer v. Brown*, 12 Am. B. R. 178; In re Henderson, *Ib.*, 351. But the orders there made proceed upon an entirely different basis, and are carefully to be distinguished. The statement of the bankrupt was simply not believed, and was therefore disregarded. They are not to be construed as undertaking to compel him to turn over what he has not, but what the court finds, notwithstanding his denials, that he in fact has."

In re Sax, 15 A. B. R. 456 (D. C. Pa.): "If it be clearly shown that a bankrupt has money or goods in his possession that belong to his trustee, he must take the consequences of a refusal to hand them over, but he should not be summarily directed to pay unless the court is morally certain that there has been concealment and that obedience to the order can be enforced. If the bankrupt has been guilty of fraudulent concealment, but no longer has the goods or the money, he should be prosecuted. He should not be imprisoned on a summary proceeding for contempt, unless he is disobeying an order with which he is able to comply."

In re Longbottom & Sons, 15 A. B. R. 437, 142 Fed. 291 (D. C. Pa.): "He does not find as a fact that * * * the bankrupts have in their possession or control the sums of money. * * * Such payments may have been preferential but this fact is not sufficient to support an order on a bankrupt to pay over money which he has already parted with in good faith to one of his creditors."

But if the bankrupt or other person proceeded against have control, it is sufficient, though he have not actual possession.⁶⁵

⁶⁵. But compare, on the facts, In re Green, 6 A. B. R. 270 (D. C. Penn.).

In re Cole, 16 A. B. R. 304, 144 Fed. 392 (C. C. A. Me.): "It also cannot be denied that a bankrupt whose funds are deposited with an agent, cannot excuse himself from not delivering over the same to the trustee because so deposited, unless he shows as a matter of fact an inability to obtain the actual possession of what he ought to surrender."

In re Dickens, 23 A. B. R. 660, 175 Fed. 808 (D. C. Ala.): "The order of the referee in this case is that the bankrupt shall turn over to the trustee in bankruptcy the sum of \$20,000. I do not find in the record sufficient evidence to justify an order requiring the bankrupt to turn over to the trustee the specific sum of \$20,000. As I understand the evidence and the contention of the petitioner, an order requiring the bankrupt to turn over \$40,000 or \$50,000, or more, might as well have been made. There is no evidence clearly or satisfactorily showing that the bankrupt had the sum of money named in his possession or control on November 4, 1909, when the order was made, or on October 26, 1909, when the petition praying said order was filed, or that he recently had such sum of money prior thereto. There is evidence in the record that at some time prior to the said dates the bankrupt was shown, in a certain proceeding in the State Chancery Court, to have been short in the sum of \$20,000 and more in his accounts with the English Manufacturing Company, of which he was the surviving partner, conducting its business. But that fact falls far short of establishing the fact that he had that sum of money in his possession on or about October 26, 1909. We may surmise from the evidence that he had that amount of money or much more in the past year or two; but conjecture, or speculation, or mere inferences, are not sufficient in this proceeding. There must be clear and convincing proof on which the court must act in making an order for contempt."

§ 1846. Similarly, Agents and Court Officers Not Subject to Summary Orders as to Disbursements Already Made.—Similarly, agents and court officers are not subject to summary orders to surrender property or assets already out of their possession or disbursed.⁶⁶

§ 1847. Likewise, No Interest to Be Included.—Likewise, interest may not be included in the summary order to surrender;⁶⁷ unless of course interest actually has been received.

§ 1848. Whether Possession at Time of Filing Summary Petition or of Granting Order, Requisite.—Nor will it, in order to obtain the order of surrender, probably suffice simply to prove that he had the possession of the assets at the time of the filing of the trustee's petition and that he has since disposed of them, he no longer having control over them or their proceeds.⁶⁸

⁶⁶. See ante, "No Summary Order as to Sums Already Disbursed," §§ 1612, 1666, 1829. In re Fogelman, 26 A. B. R. 742, 188 Fed. 755 (D. C. N. Y.); In re Denson, 28 A. B. R. 158, 195 Fed. 854 (D. C. Ala.).

⁶⁷. In re Davis, 9 A. B. R. 670 (D. C. Tex.).

⁶⁸. In re Rosser, 4 A. B. R. 153, 101 Fed. 562 (C. C. A. Mo.).

Inferentially, In re Leinweber, 12 A.

B. R. 175 (D. C. Conn.), where the court finds he continued to have possession up to the time the order was made.

Impliedly, In re Adler, 12 A. B. R. 19, 129 Fed. 502 (D. C. Tenn.); In re Friedman, 2 A. B. R. 301 (Ref. N. Y.); also, inferentially, In re Greenberg, 5 A. B. R. 840 (D. C. N. Y.).

Contra, impliedly, In re Kurtz, 11 A. B. R. 129 (D. C. Penn.), in which case

Inferentially, *In re Purvine*, 2 A. B. R. 787 (C. C. A. Tex.): "It is implied that the party has the ability to obey the order."

Inferentially, *In re Alphin & Lake Cotton Co.*, 14 A. B. R. 194 (D. C. Ark.): "If the money is once traced into the hands of a respondent, the burden is upon him to make some reasonable explanation of what became of it, or at least that it has ceased to be in his possession or under his control at the time the order to turn it over is made."

Although, of course, he can be punished for contempt for having thus disposed of them in the meantime.

§ 1849. Circumstantial Evidence Sufficient.—It is not necessary that the possession of the concealed assets be proved by the direct evidence of those who actually saw—circumstantial evidence is sufficient, if strong enough.⁶⁹

In re Cole, 16 A. B. R. 303, 144 Fed. 392 (C. C. A. Me.): "* * * may be supported by a mere preponderance of evidence, presumptions or inferences."

Obiter, *In re Felson*, 10 A. B. R. 716, 124 Fed. 288 (D. C. N. Y.): "In order to justify an order that the bankrupt pay over money or deliver property, it is not necessary that the evidence show clearly and distinctly that the bankrupt has the money or the property in his possession in such shape, or in such a location, that witnesses have seen it, and may, therefore, testify that the bankrupt actually has the money or property in his possession at some particular place. It is sufficient if the evidence discloses the fact that at a certain date the bankrupt had the property or the money in his possession and has not lost the same by fire or other casualty, for which he is not responsible, or has not expended the same in gambling or in some other manner."

Indeed, the question most usually arises with regard to stocks of merchandise or their proceeds where it is next to impossible to prove by eye witnesses that the debtor still has possession or control of the proceeds. Proof of such possession or control most frequently is simply a deduction from a multitude of circumstances, usually derived largely from the statements of the debtor himself, upon cross-examination, in his efforts to explain the disappearance of assets.⁷⁰

§ 1850. Presumption of Continued Possession When Property Once Traced and Shortage Unexplained.—If it is proved that the debtor recently had the possession, then the presumption that he still has possession will follow, unless he reasonably accounts for the disposition or disappearance of the assets.⁷¹

it distinctly appears that the bankrupt had actually spent the money after the bankruptcy, yet the court ordered him to refund it.

69. Instance, alleged payment to mother, *In re Feldser*, 14 A. B. R. 217, 134 Fed. 307 (D. C. Penn.). [1867] *In re Goodridge*, Fed. Cas. 5,547.

70. Compare, as to weakness of such deductions, cases cited at end of next section under "Limitations of Rule."

For instances where the present possession of assets has been decided by comparison of purchases, sales, financial statements, inventories, etc., and discrepancies unsatisfactorily explained, etc., see the cases cited under the next section following.

71. *In re Rosenthal*, 29 A. B. R. 515, 200 Fed. 190 (D. C. N. Y.); *In re Meier*, 25 A. B. R. 272, 182 Fed. 799 (C. C. A. Mo.).

Thus, where the court is satisfied that property came into the hands of the bankrupt shortly before the adjudication, and the schedules give no account of the property or its proceeds, and the bankrupt fails to make any credible explanation on his examination or elsewhere showing what has become of such property, the court is authorized to consider the property or its proceeds still in the control of the bankrupt and to require that it be produced and surrendered to the trustee.⁷²

In *re Meier*, 25 A. B. R. 272, 182 Fed. 799 (C. C. A. Mo.): "The settled rule is that, when property of a bankrupt estate is traced to the possession of one

⁷² Instance, *In re Deuell*, 4 A. B. R. 60, 100 Fed. 633 (D. C. Mo.); *obiter*, *In re Felson*, 10 A. B. R. 716, 124 Fed. 288 (D. C. N. Y.); *In re Schlesinger*, 3 A. B. R. 342, 97 Fed. 930 (D. C. N. Y.), affirmed in 4 A. B. R. 361, 102 Fed. 117. Compare, to same effect, *In re Finkelstein*, 3 A. B. R. 800, 101 Fed. 418 (D. C. N. Y.); *In re Greenberg*, 5 A. B. R. 840, 106 Fed. 496 (D. C. N. Y.), in which case the court found so much false testimony that it was even in doubt whether there was as much assets in the bankrupt's hands as the necessary deductions from the testimony might warrant—the bankrupt evidently had perjured himself to such an extent that even his admissions against interest were discredited.

Obiter, *In re Mayer*, 3 A. B. R. 533, 98 Fed. 839 (D. C. Wis.); *In re Anderson*, 4 A. B. R. 640, 103 Fed. 854 (D. C. S. Car.); *In re Goldfarb Bros.*, 12 A. B. R. 386 (D. C. Ga.); instance, *In re Wilson*, 8 A. B. R. 612, 116 Fed. 419 (D. C. Ark.); *In re Rosser*, 4 A. B. R. 153, 101 Fed. 562 (C. C. A. Mo.).

In re DeGottardi, 7 A. B. R. 723, 114 Fed. 328 (D. C. Calif.), where an alleged burglarizing of the bankrupt's store was the excuse, accompanied by unwillingness and refusal of the bankrupt to answer questions, etc.

Obiter, *In re Milk Co.*, 16 A. B. R. 732 (D. C. Penn.), quoted ante, § 1845. Instance, alleged robbery, *In re Herschkowitz*, 14 A. B. R. 86 (D. C. N. Y.).

In re Frankfort, 15 A. B. R. 210 (D. C. N. Y.), in which pocketbook snatching from a street car was alleged.

In re Levin, 6 A. B. R. 743 (Ref. N. Y., affirmed in D. C.), wherein robbery of the bankrupt's store and loss of \$10,000 was alleged, but the statement to the police at the time was that practically nothing had been taken.

Instance, uncorroborated testimony of bankrupt as to losses by gambling and dissipation, *In re Henderson*, 12 A. B. R. 351, 130 Fed. 385 (D. C. Penn.).

Instance, alleged gambling, the explanation, *In re Friedman*, 2 A. B. R. 307 (Ref. N. Y.).

Instance, *In re Weinreb*, 16 A. B. R. 702, 146 Fed. 243 (C. C. A. N. Y.).

Instance, fictitious claim of payment of part of proceeds of sale to mother, *In re Feldser*, 14 A. B. R. 217, 134 Fed. 307 (D. C. Penn.).

Compare, on analogous proposition of concealment as a bar to discharge, the following cases: *In re Leopold*, 5 A. B. R. 279 (Ref. N. Y.); *In re Meyers*, 2 A. B. R. 707, 96 Fed. 408 (D. C. N. Y.); *In re Crossman*, 6 A. B. R. 510, 111 Fed. 507 (D. C. Mich.); *In re Friedman*, 2 A. B. R. 301 (Ref. N. Y.), alleged robbery; *In re Leinweber*, 12 A. B. R. 175, 128 Fed. 641 (D. C. Conn.).

In re Lesaius, 21 A. B. R. 23, 163 Fed. 614 (D. C. Pa.); *In re Leverton*, 19 A. B. R. 426 155 Fed. 925 (D. C. Pa.); *In re Friedman*, 18 A. B. R. 712, 153 Fed. 939 (D. C. N. Y., affirmed in 20 A. B. R. 37), quoted at § 1863; *Seigel v. Cartel*, 21 A. B. R. 140, 164 Fed. 691 (C. C. A. Iowa), quoted at § 2501½; *Kirsner v. Taliaferro*, 29 A. B. R. 832, 202 Fed. 51 (C. C. A. Va.); *obiter*, *In re Epstein*, 30 A. B. R. 387, 206 Fed. 568 (D. C. Pa.); instance, *Shea v. Lewis*, 30 A. B. R. 436, 206 Fed. 877 (C. C. A. Minn.); instance, *In re Belluscio*, 25 A. B. R. 660 (Ref. N. Y.).

In one case it was stated that as a rule, the presumption of possession by the bankrupt arising from his failure to account for property traced to his recent custody, is applicable only in those jurisdictions wherein it is held that the bankrupt has the burden of proving his innocence. *In re Haring*, 27 A. B. R. 285, 193 Fed. 168 (D. C. Mich.).

But compare [on review, however, of contempt order rather than of order for surrender of assets] *Stuart v. Reynolds*, 29 A. B. R. 412, 204 Fed. 709 (C. C. A. Ala.), quoted at § 1845.

who receives it upon the eve of the bankruptcy of its owner, it is presumed to remain in his possession or under his control until he satisfactorily accounts to the court of bankruptcy for its disposition or disappearance; that the burden is upon him to satisfactorily so account for it; and that he cannot escape an order for its surrender by simply denying under oath that he has it, or that it is the property of the bankrupt estate." Quoted ante, § 1843.

In *re Levy & Co.*, 15 A. B. R. 168, 142 Fed. 442 (C. C. A.): "It was open to them to explain the apparent discrepancy by proof that some of the property did not actually come into their hands or that it was sold at a price below the inventory value, especially as the firm was on the eve of bankruptcy, or that the statements were, for some other reasons, inaccurate."

In *re Cotton Co.* (Alphin & Lake Cotton Co.), 14 A. B. R. 194, 134 Fed. 477 (D. C. Ark.): "If the money is once traced into the hands of a respondent, the burden is upon him to make some reasonable explanation of what became of it, or at least that it has ceased to be in his possession or under his control at the time the order to turn it over is made."

In *re McCormick*, 3 A. B. R. 340, 97 Fed. 566 (D. C. N. Y.): "As respects the sum of \$1500 ordered to be paid to the trustee, the explanation given by the bankrupt that he carried that money in his trousers pocket for some two or three weeks until he lost it by having his pocket picked upon an Eighth avenue car, after a visit to Coney Island, though quite possible in itself, is accompanied by such improbable circumstances stated by him as occurring before and after that it is difficult to be credited."

In *re Royce Dry Goods Co.*, 13 A. B. R. 266, 133 Fed. 100 (D. C. Mo.): "Making every reasonable allowance based on the evidence, there was at the time the company made its assignment, the 4th day of January, 1904, a discrepancy between the property W. K. Royce stated in writing to have been on hand November 30, 1903, of at least \$25,000. What became of this difference? The presumption of law in such cases, in the absence of satisfactory explanation, is that the property traced to the hands of the bankrupt a short time prior to the suspension of business remains in his hands, and the bankrupt must answer therefore."

In *re Averick*, 22 A. B. R. 518, 170 Fed. 521 (D. C. Pa.): "As shown by his bills and invoices, he had bought for the fall trade goods to the amount of \$10,427.19; and had on hand at the beginning of the season, as found by the referee, stock in the two stores of the value of \$5,000, \$4,000 at Susquehanna and \$1,000 at Sidney. He paid out some \$3,025 to creditors on various accounts in the three months preceding his bankruptcy, and had \$1,100 of other cash expenses; besides losing \$300 by sales on credit. These figures show \$4,202.19 worth of goods unaccounted for, which the bankrupt must either have in his possession and keep back from his trustee, or else have disposed of them and put the money in his pocket. The conclusion so reached depends of course on the evidence and the deductions made from it, of which there can be no just criticism, provided the figures taken are accurate. That brand new goods of over \$10,000 went into these stores within the few months immediately preceding bankruptcy is not and cannot be denied, being proved by the bills or invoices. * * * The value of the goods which the bankrupt had when he failed is put in the schedules, where he would be inclined to make the most of them, at \$6,800. According to the appraisers they were worth only \$4,800, and they were sold by the trustee the latter part of January, after taking out the \$300 exemption, at \$3,900. It is now claimed, that at cost prices with which comparison is to be made, they were worth \$7,600. But all things considered, the estimate of the bankrupt, when he made up his schedules, may well be taken. There was

no controversy then, as there is now, and he had no purpose to serve in fixing the value except possibly to enhance it. * * * What is there, then, to relieve the bankrupt from the logic of the situation? He lost no money by speculation, bad investments, or gambling. He had no bad debts outside of the \$300 already allowed him. Neither his store nor his personal expenses were large, and all that he paid out on this account as well as on business debts or for borrowed money has been credited. The amount of goods which he bought was altogether beyond the needs of his business, and having been received within three or at most four short months, immediately preceding his bankruptcy, had disappeared at the end of that time with almost nothing to show for it. He could not have sold them in the ordinary course of trade, his business not being large enough to take them. And if he disposed of them at forced sales it would have been known and attracted attention. It is this that constitutes the strength of the case against him and gives an adverse cast to his so-called failure. All things considered, the only fair conclusion with the figures so seriously against him as they are, is that he covertly made away with so much as he cannot account for, and should now in consequence be required to produce and turn it over."

Ripon Knitting Wks. v. Schreiber, 4 A. B. R. 299, 101 Fed. 810 (D. C. Wash., affirmed in 101 Fed. 1006): "The decision of the court that the bankrupt has at least \$3000 in his possession or under his control is based upon convincing evidence to the effect that a large amount of money actually came into his possession within a few months before the adjudication. Of the money so received, more than \$2000 remains entirely unaccounted for after giving full credit for all expenditures shown by the respondent's books of account, and after allowing in full the extravagant amount which he claims to have used for his personal expenses, and in dissolute practice, and losses in gambling. As to so much of the money, this is not a case of failure to give a satisfactory account, or to show in a satisfactory way how it has been disposed of, but it is a case of total failure to account in any way whatever, or to give any explanation. I am also convinced that the amount which the respondent claims to have lost in gambling is considerably in excess of the total amount of his actual losses. I am also convinced that, with a deliberately formed intention to defraud his creditors, the respondent proceeded methodically to make liberal purchases of merchandise on credit, and to dispose of his stock for cash as rapidly as possible. During the spring and summer months he conducted a slaughter sale, selling goods so much below the market value as to create a rush of business."

In *re Gerstel*, 10 A. B. R. 412, 413, 123 Fed. 166 (D. C. Ills.): "The rule in these cases is that the answer of the respondent is not conclusive on the court; that the court may proceed to inquire into the facts, and where it has been shown that property has come into the hands of the bankrupt shortly before the adjudication, that the schedules give no account either of this property or its proceeds, and that the bankrupt, by answer or by examination under oath, fails to make any credible explanation, showing what became of such property, the court, when so satisfied, is authorized to consider the property or its proceeds as being still in the possession or under the control of the bankrupt, and to require by order that it be produced and delivered to the trustee, and, upon failure to obey such order, to punish by imprisonment for contempt."

In *re Lasky*, 20 A. B. R. 729, 163 Fed. 99 (D. C. Ala.): "From the above-cited cases it seems clear to my mind that the following principle of law is well settled, to wit: That the property of a bankrupt estate, traced to the recent control or possession of the bankrupt, is presumed to remain there until he satisfactorily accounts to the court for its disposition or disappearance. Now let

us see what may be properly deduced from the evidence as showing the property to be in the bankrupt's possession during the five months next before his adjudication:

A stock of goods on hand worth at least.....	\$2,500 00
Goods purchased within the five months for which not a dollar was paid	6,500 00
	<hr/>
	\$9,000 00

How and for how much of this does he account? First: He says that all goods were sold and converted into cash. The evidence indicates that they brought about cost, but let us allow \$2,000 for his selling cheap and the little remnant left in the store, so we have:

Item 1. Discount to get quick sales.....	\$2,000 00
Item 2. (He gives in detail his cost of doing business, and under that evidence \$100 a month is a liberal allowance, so) expenses of running store were.....	500 00
Item 3. (His checks show exactly what he paid on old accounts, freight, and drayage in these five months.) Paid for goods, freight, and drayage about.....	1,300 00
Item 4. Goldberg's living expenses, \$200 per month.....	1,000 00
Item 5. Lasky's living expenses, \$200 per month.....	1,000 00
Item 6. Accident to sister.....	500 00
Item 7. Mother's and sister's trips.....	300 00
Item 8. Money which Mr. and Mrs. Goldberg took away for living expenses, about	300 00
	<hr/>
Total	\$6,900 00

This resolves every doubt in the bankrupt's favor and is more liberal to him than are the reported cases. It shows \$2,100 coming into his possession and wholly unaccounted for, and the estimate made by the court certainly not overdrawn and, if anything, is rather below what may be sustained by the evidence. It is not attempted to state the exact amount of the bankrupt's frauds and concealments. The law does not require this, for, as is said in *In re Schlesinger* (D. C.), 3 Am. B. R. 342, 97 Fed. 930: 'A debtor is not, however, to go scott-free because the exact amount of his frauds and concealments are not ascertainable, nor should the Bankrupt Act be suffered to be paralyzed as respects the creditors by such means.' A merchant should not be permitted to shut his eyes to the disappearance of his goods, and when called upon by the court to account therefor escape the penalty of the law by simply saying: 'I have not the goods. I have no money.'"

In re Kane, 10 A. B. R. 478, 125 Fed. 984 (D. C. Pa.): "Money having been traced directly into his hands, he cannot swear himself free from liability by any such general and sweeping statement."

In re Shachter, 9 A. B. R. 499 (D. C. Ga.): "The present case measures up exactly to the rule stated by Judge Sanborn (in concurring opinion in *Boyd v. Glucklich*, 8 A. B. R. 393, 116 Fed. 131) as follows: 'The rule by which this issue is to be determined is that the property of the bankrupt estate traced to the recent possession or control of the bankrupt is presumed to remain there until he satisfactorily accounts to the court for its disposition or disappearance.'"

In re Epstein, 15 A. B. R. 711 (D. C. Penn.): "Where it is shown that the

bankrupts have purchased goods to the extent of \$20,000 within three months of their bankruptcy and have no other explanation to give of the disappearance of large sums of money traced to their hands than a general denial, entirely unsupported by facts or credible circumstances, the referee is justified in finding that property has been concealed and an order to pay will be sustained."

In *re Fidler & Son*, 21 A. B. R. 101, 163 Fed. 973 (D. C. Pa.): "The bankrupts have absolutely no explanation to offer for this large discrepancy. Their attention being called to it, that was the express answer which they gave. They admittedly experienced no loss by theft nor by fire, and, doing a cash and not a credit business, as they claim, they had no bad debts, if any could have accumulated in the short time in question. Indeed they even go so far as to say that they did not know that they were insolvent, and only went into bankruptcy because suits were being brought against them. But \$8,000 worth of goods, obtained inside of three short months, if their bills are to be relied on, are not to be disposed of upon any such convenient lack of knowledge. They certainly could not have disappeared through the ordinary and legitimate channels without leaving some trace behind them."

In *re Cramer*, 23 A. B. R. 637, 175 Fed. 879 (D. C. Mass.): "The bankrupt may have been, as the referee thinks, a person of an extremely low order of intelligence; but there is no question that he had intelligence enough to carry on business as a wholesale and retail dealer in picture frames for five years in Worcester, not to mention," etc. "The purchases of goods on credit and their subsequent disappearance, or the disappearance of money received from them, if sold, within so short a time before the bankruptcy and while the bankrupt knew he was insolvent, together with the entire failure of the bankrupt to meet by reasonable and honest explanation the presumption against him which these facts create, would to my mind go very far, without more, to prove him guilty, of concealment. If, under the pressure of an inquiry into these doings of his, he has also made admissions of the kind testified to by the trustee, I am unable to believe that justice will be done if the case be treated as one wherein the power of the court to compel restitution of what is being dishonestly withheld from creditors cannot be exercised for want of sufficient evidence. The order denying the trustee's petition is disapproved, and is to be vacated. On the case as now presented, the referee, in my judgment, should make such an order as has been requested by the trustee."

And the same rules prevail where it is traced into the hands of an agent of the bankrupt.⁷³

But see, limitations of rule.^{73a}

In *re Adler*, 12 A. B. R. 19, 129 Fed. 502 (D. C. Tenn.): "The fact that he accounts falsely for his dissipation of the money, the fact that he does not satisfactorily disclose his uses of it, the fact that he evades the exhibition of his conduct in the premises, may indicate that he has defrauded his creditors, that he has dealt falsely with them, that he has egregiously perjured himself and forsworn the truth, and may invoke other remedies under the

⁷³. Instance, In *re Friedman*, 13 A. B. R. 712, 153 Fed. 939 (D. C. N. Y.), affirmed in 20 A. B. R. 37, 161 Fed. 260, C. C. A.), quoted at § 1863.

^{73a}. And compare concurring opinion in *Stuart v. Reynolds*, 29 A. B. R.

412, 204 Fed. 709 (C. C. A. Ala.), quoted at § 1845, this case being, however, a review of an order of contempt and not for surrender of assets.

statute; but not this of a peremptory order to pay the money to the trustee, and punishment by contempt for failure to do so."

In *re Idzall*, 2 A. B. R. 741, 96 Fed. 314 (D. C. Iowa): "The mere fact of inability to account for money or property in possession of the bankrupt shortly prior to his bankruptcy does not itself show concealment of it."

In *re Sax*, 15 A. B. R. 456 (D. C. Pa.): "I do not deny that the bankrupt, who is certainly not a literate person has probably failed to account satisfactorily for some of the merchandise that went into his business during the year before his failure, but calculations and estimates based on such uncertain evidence as is now before the court are not reliable enough to justify an order that may send a man to jail for an indefinite period."

In *re Switzer*, 15 A. B. R. 470, 140 Fed. 976 (D. C. S. Car.): "The very earnest and learned counsel for the creditors has pressed very strongly for said exercise of authority, claiming that, in the nature of things, it is impossible for him to offer direct testimony showing that the bankrupt is in possession of goods or money; and his case, briefly stated, is that, having shown that the bankrupt was in possession of a certain stock of merchandise at a time stated, and that at the time he was adjudged bankrupt his stock of merchandise was only of a certain value, and that he has only shown payments of a given amount, it should follow as a conclusion of law that he is in the actual possession of all that he has not accounted for. If this rule was generally applied, scarcely any bankrupt would escape a like proceeding, for it is very rare that a bankrupt can satisfactorily account for everything which he ought to have in his possession and which he has not, and the result would be that the judge, under the guise of proceedings for contempt, could be called upon to try without a jury nearly every man who passes through the court of bankruptcy."

In *re Lesaius*, 21 A. B. R. 23, 163 Fed. 614 (D. C. Pa.): "It is also to be kept in mind that the object is to recover tangible property, and not to punish as on indictment for a fraudulent concealment or abstraction."

In *re Rogowski*, 21 A. B. R. 553, 166 Fed. 165 (D. C. Ga.): "If the rule be adopted, announced in some cases, that where a bankrupt shortly before his failure has on hand a large stock of merchandise, and when proceedings in bankruptcy are instituted he is found to have but a small amount of goods, the stock being depleted to such an extent that it could not have occurred in the ordinary course of business, and there are circumstances to indicate that the goods have been purposely and fraudulently removed so as to prevent their going into the hands of the trustee in bankruptcy, that then the court may require the bankrupt to produce the goods or give some reasonable explanation of their disappearance, and on his failure so to do may hold him for contempt, then a case is made out by the record here. See concurring opinion of Sanborn, Circuit Judge, in *Boyd v. Glucklich*, 8 Am. B. R. 393, 116 Fed. 131-142, 53 C. C. A. 451, and cases cited. On the other hand, if the rule be that, notwithstanding such condition of things as indicated above, the receiver, trustee, or creditor proceeding against the bankrupt is unable to point out any particular property or cash so removed, and its location, definitely and specifically, contempt proceedings are not justified, then no case is made here. I think the latter rule has been adopted by the Circuit Court of Appeals for this circuit in *Samel v. Dodd*, 16 Am. B. R. 163, 142 Fed. 68, 73 C. C. A. 254."

And where reasonable accounting is made, no order will be granted.

In *re Reese*, 22 A. B. R. 521, 170 Fed. 986 (D. C. Pa.): "This shows a difference of \$150.00 against the bankrupt, but must be regarded as practi-

cally balancing. Depending as it does on mere estimates, on one side and the other, it cannot be expected to come out even. And it is only in any case of this kind, where there are great discrepancies which cannot be explained except on the basis that the bankrupt has made away with his property, that the matter can be laid hold of by a summary order. Being satisfied therefore that the bankrupt has cleared himself in the present instance of the charge made by the trustee of withholding and appropriating what belongs to his creditors. The exceptions are sustained, and the petition of the trustee is dismissed."

§ 1851. Rejecting Improbable Explanations.—And the court is not debarred from using its own common sense in rejecting testimony that seems to it improbable.⁷⁴

Schweer v. Brown, 12 A. B. R. 181, 130 Fed. 328 (C. C. A. Ark.): "In proceedings of this character no punishment can be inflicted for reprehensible and dishonest conduct, but, in a careful effort to avoid such result, a court, when called upon to pass upon the weight of testimony and the credibility of witnesses, is not to be deprived of those faculties of judgment and discrimination as to what is true or probable on the one hand, and untrue, improbable, or absurd, upon the other, which are permitted to be exercised by juries in similar cases."

In re Deuell, 4 A. B. R. 60, 100 Fed. 634 (D. C. Mo.): "When asked if she did not talk this matter over with her husband and son, who were assisting her in running the store, and ascertain what explanation they gave, or as to what theory they had to account therefor, her answer was equally uncertain and indefinite. As the goods were not on hand when she was declared a bankrupt and as she claims the goods had not been spirited away, and testifies that they had been received and sold, the conclusion is irresistible that she must have the money in her possession, or that she knows who did receive it, and who has it. The business was conducted in her name. She thus published to the world that she was capable of transacting business, and she obtained credit for these goods upon the faith of her credibility and business capacity. Shall she be permitted thus to obtain property of other people, secrete and appropriate it, without even so much as rendering any intelligent account thereof, and escape the pains and penalties imposed by the bankrupt law, simply because she is a woman, and under the naked assumption, or bare possibility, that the husband and son embezzled the proceeds of these goods? When she assumed the office of a tradesman she became amenable to its obligations and responsibilities."

In re Lasky, 20 A. B. R. 729, 163 Fed. 99 (D. C. Ala.): "In a proceeding of this character, it is not within the province of the court to inflict punishment for dishonest conduct; but, in a careful effort to avoid such result, a court, when called to pass upon the weight of testimony and the credibility of witnesses, is not to be deprived of those faculties of judgment and discrimination as to what is true and probable, on the one hand, and untrue and improbable or

⁷⁴ *Obiter*, *In re Milk Co.*, 16 A. B. R. 732 (D. C. Penn.); instance, *In re Frankfort*, 15 A. B. R. 210 (D. C. N. Y.); instance where no explanation offered, *In re Fidler & Son*, 21 A. B. R. 101, 163 Fed. 973 (D. C. Pa.); *Seigel v. Cartel*, 21 A. B. R. 140, 164 Fed. 691 (C. C. A. Iowa), quoted at § 2649; *In*

re Friedman, 21 A. B. R. 213, 164 Fed. 131 (D. C. Wis.), quoted at § 852; *In re Holland*, 23 A. B. R. 835, 176 Fed. 624 (D. C. N. Y.); *In re Cramer*, 23 A. B. R. 637, 175 Fed. 879 (D. C. Mass.); *In re Meier*, 25 A. B. R. 272, 182 Fed. 799 (C. C. A. Mo.).

absurd, upon the other, which are permitted to be exercised by juries in similar cases."

In *re Kane*, 12 A. B. R. 444 (D. C. N. Y.): "Having regard to what is involved it is to be exercised with caution; but where a proper case is presented by the evidence, the court is not to allow itself to be deceived by evasions nor deterred by the consequences."

Instance, In *re Weinreb*, 16 A. B. R. 702, 146 Fed. 243 (C. C. A. N. Y.): "This story is extremely improbable [accounting for assets by saying had purchased \$18,200 smuggled diamonds from a stranger]. Of course, smuggled goods may be purchased, and, if purchased, the acts of the parties engaged in such a business are frequently stealthy and furtive. But if that is the explanation of the circumstances of this purchase, it is not enough for the bankrupts to simply say so. Their story, if true, could be corroborated in various ways. But it is entirely uncorroborated. It is precisely the kind of a story which bankrupts would tell, who had been engaged in the diamond business, and had been planning a fraudulent bankruptcy and had drawn \$18,000 in cash just before their bankruptcy, for the purpose of concealing it from their creditors. I cannot avoid the conclusion that their story is an entire fabrication, and that the bankrupts have this money concealed from their creditors, and that they should be ordered to pay it to the trustee."

Instance, In *re Friedman*, 18 A. B. R. 712, 153 Fed. 939 (D. C. N. Y.) affirmed in 20 A. B. R. 37, 161 Fed. 260 (C. C. A.): "The story of Celia Friedman is inherently preposterous, as well as demonstrably false."

[1867] In *re Goodridge*, Fed. Cas. 5,547: "A fraud of this kind here alleged is one that can seldom be proved by other than circumstantial evidence. The parties to the transaction are generally, as in this case, the only witnesses, and if their stories are to be believed as told, no fraud can be established. External evidence is not to be had, and the truth must be reached by examining the evidence of the alleged parties to the fraud, and weighing its probabilities, and scrutinizing its general tenor and manner. * * * The determination of the question of fraud or no fraud must, under such circumstances, depend upon the impression made by the evidence of the parties concerned. Of course, those who would commit such a fraud, would swear falsely to carry it through. If their positive testimony to the honesty of the transaction is overborne by badges and indicia of fraud, deduced from their own testimony, the conclusion must be that there was fraud."

Thus, as to evasive answers, and repetitions of "I don't remember," or "I don't know," as to matters naturally within the witness' knowledge.⁷⁵

In *re Schlesinger*, 3 A. B. R. 342, 97 Fed. 930 (D. C. N. Y., affirmed in 4 A. B. R. 361, 102 Fed. 117): "The bankrupt kept no books of account. The check book was not produced, and all checks returned were destroyed. No account could be extracted from him as to what was done with these moneys, except

⁷⁵ In *re Alphin & Lake Cotton Co.*, 14 A. B. R. 194, 134 Fed. 477 (D. C. Ark.); In *re Kurtz*, 11 A. B. R. 129 (D. C. Penn.), wherein a bank deposit as "Manager" was found to be the bankrupt's own money. In *re Epstein*, 15 A. B. R. 711 (D. C. Penn.). Instance, *Moody v. Cole*, 17 A. B. R. 825 (D. C. Me.).

Instance, *Ohio Valley B'k v. Mack*, 20 A. B. R. 919, 163 Fed. 155 (D. C. Ohio), quoted at § 554. Instance, where explanations accepted, In *re Walder*, 16 A. B. R. 42 (D. C. Conn.). See ante, § 1568; post, § 2331.

For further instances, see cases cited under preceding section, and on the subject of discharge, post, §§ 2649, 2650.

that they were paid out. To all enquiries for particulars, his answer was 'I don't know' or 'I don't remember.' * * * The ignorance he professed in regard to the disposition of his money is altogether incredible. I cannot regard his testimony on this subject as other than a tissue of perjuries. The destruction of vouchers while his papers in bankruptcy were preparing, is not consistent with any other inference than the intent to conceal the facts and defraud his creditors."

But the court need not refuse to accept admissions against interest as proof, simply because the bankrupt is such an enormous liar that even his testimony, adverse to his own interest, is of doubtful reliability—he should not escape through excessive falsehood.⁷⁶

Compare, to this effect, *Murray v. Joseph*, 16 A. B. R. 717, 146 Fed. 260 (D. C. N. Y.): "A trustee in bankruptcy has to do the best he can, and it would not do in such cases if you formed an unfavorable opinion of any of the witnesses to simply say you cannot put any reliance in such evidence, and thereby won't decide anything. It is just this class of cases in which it is the duty of the jury to investigate the case carefully and see that justice is done."

Failure to produce important witnesses is an indication of falsehood.⁷⁷

§ 1852. No Presumption of Continued Possession if Circumstances Raise Counter Presumption.—If, from the nature of the circumstances, an equal presumption of loss or expenditure arises, the presumption of continued possession, of course, will not prevail. Thus, simply to prove that a business man received a consignment of goods would not raise a presumption that he still has them, for the circumstances would of themselves raise the offsetting presumption that these goods were sold. The presumption of continued possession is, then, only as strong as the nature of the circumstances permits. Thus, property in a wife's possession is not presumptively also in the bankrupt husband's control, and a summary order on the bankrupt is improper where the proof shows the bankrupt's wife still in possession of the assets, claiming to have received them from the bankrupt in repayment of a loan, even though the loan was fictitious, there being no presumption that the assets are still within the bankrupt's control from the mere fact that they are in the hands of his wife. The wife is also an adverse claimant and she cannot be denied the right to a plenary action to determine her right to the assets, by an order on her husband which she might feel she ought to aid him in obeying.⁷⁸

⁷⁶. But compare, *In re Lesser*, 8 A. B. R. 12, 114 Fed. 83 (C. C. A. N. Y.).

⁷⁷. Instance, *Moody v. Cole*, 17 A. B. R. 82 (D. C. Me.); *In re Mayer*, 19 A. B. R. 480, 156 Fed. 432, 157 Fed. 836 (D. C. Pa.), quoted at § 554½.

⁷⁸. *In re Green*, 6 A. B. R. 270 (D. C. Penn.).

Statements to commercial agencies of assets are not necessarily to be taken as conclusive admissions against the bankrupt of the existence of the as-

sets if the evidence is unsatisfactory upon the point that the assets ever actually existed to the amount stated. Compare, *In re Lesser*, 8 A. B. R. 12, 114 Fed. 83 (C. C. A. N. Y.).

In re Adler, 12 A. B. R. 19, 129 Fed. 502 (D. C. Tenn.), where the bankrupt, however, himself said the statements "were untrue."

Refusal because of Incrimination.—The bankrupt may file a special plea to the petition for such an order, upon

§ 1853. Order to Describe Property—Orders to Pay Value of Goods, Alternative Orders, etc.—The order for surrender must describe definitely the property to be surrendered.⁷⁹

Samel v. Dodd, 16 A. B. R. 167, 142 Fed. 68 (C. C. A. Ga.): "The order should describe the property with reasonable certainty in order to assure its identity, and the command of the court to the bankrupt should be to surrender the very property sought to be recovered."

The order should follow the pleadings as to the description of the property.⁸⁰

Lesaius v. Goodman, 21 A. B. R. 446, 165 Fed. 889 (C. C. A. Pa.): "The other issue presented the question as to whether the bankrupt had fraudulently retained \$10,000, or any part of that sum. The court's order, however, does not deal with that issue. It directs the bankrupt, not to pay over \$4,000 which he has fraudulently retained, but to deliver 'gentlemen's furnishings and clothing to the extent and of the value of \$4,000.' We think the order is not supported by the pleadings, and that it must be reversed."

It has been held, indeed, that the order should not be to pay the "value" of the goods: that the finding should not be so indefinite as not to show in what form the property exists at the present time.

Samel v. Dodd, 16 A. B. R. 167, 142 Fed. 68 (C. C. A. Ga.): "It is thus observed that the court found goods, wares and merchandise to be in possession of the bankrupts, and, in effect, rendered judgment for their value, and ordered the commitment of the bankrupts until the amount should be paid. We are of opinion that the order cannot be sustained. If the bankrupts had in their possession merchandise, which should have been delivered to the trustee, the appropriate order would have been for the delivery of merchandise. If they had money, which formed part of their estate, they should have been required to pay over money. * * *

"But it is not within the power of the court, in such a proceeding, to render judgment for the value of the property ascertained to be in the possession of, and contumaciously withheld by, a bankrupt, and attach for contempt upon his refusal to pay. Such procedure would approach dangerously near the line, if it did not overstep it, of imprisonment for debt. * * *

"It seems to me that any evidence that conclusively showed they presently had in possession and control either the money or the goods would necessarily

the ground that to require him to answer thereto would tend to subject him to criminal prosecution, *In re Glassner, et al.*, 8 A. B. R. 184 (Ref. Md.).

But the bankrupt may not refuse to surrender "documents" title to which is vested in the trustee, because they might furnish incriminating evidence against himself. See ante, § 1558.

And he must produce them for inspection in court for the court to ascertain whether incriminating evidence is contained therein and must not wholly refuse to produce the documents. See ante, § 1560.

Withholding Discharge until Suffi-

cient Accounting Made.—In several cases the courts have assumed the doubtful power of withholding a discharge until the bankrupt has made a sufficient accounting, even where the facts were not sufficient to bar discharge nor to warrant an order upon the bankrupt to turn over property. *In re Walther*, 2 A. B. R. 702, 95 Fed. 941 (D. C. N. Y.).

79. Compare, *In re Lesaius*, 21 A. B. R. 23, 163 Fed. 614 (D. C. Pa.); *In re Rogowski*, 21 A. B. R. 553, 166 Fed. 165 (D. C. Ga.), quoted at § 1850.

80. *Samel v. Dodd*, 16 A. B. R. 169, 142 Fed. 68 (C. C. A. Ga.).

show where the same was kept or deposited, so that it could be reached by the process of the bankruptcy court, or of some court in a suit by the trustee."

In *re Lesaius*, 21 A. B. R. 23, 163 Fed. 614 (D. C. Pa.): "The order it may be should be to turn over the goods, and not in the alternative to pay the value, the proceedings, as just stated, being supposed to be directed to the recovery of specific property. * * * But that does not prevent its being measured by its value; that being the only way to indicate the extent of it. Neither is it necessary to do more than describe the property generally, as consisting for instance in the present case of gentlemen's furnishings and clothing, such as the bankrupt was carrying. To require greater particularity would make such proceedings practically nugatory. * * * This would not be necessary even to convict upon indictment."

The rule has even been laid down, though too strictly, that there must be a finding not only of the precise property but also of its location.

In *re Rogowski*, 21 A. B. R. 553, 166 Fed. 165 (D. C. Ga.): "On the other hand, if the rule be that, notwithstanding such condition of things as indicated above (unexplained and abnormal shrinkage of assets on the eve of bankruptcy) the receiver, trustee or creditor proceeding against the bankrupt is unable to point out any particular property or cash so removed, and its location, definitely and specifically contempt proceedings are not justified, then no case is made here. I think the latter rule has been adopted by the Circuit Court of Appeals for this circuit."

And the order should not be made unless the goods can be followed and be sufficiently identified to enable the marshal to seize them.⁸¹

However on review, if the record does not contain the evidence, yet the Circuit Court of Appeals will presume from the fact that the order was granted to pay over money, that the property was money and that it was shown to be still in the bankrupt's control.⁸²

§ 1854. Review of Summary Orders—Set Aside Only for Manifest Error.—On review of a referee's summary order, the District Court will not set aside the order except in case of manifest error.⁸³

Impliedly, In *re Cole*, 14 A. B. R. 389, 133 Fed. 414 (D. C. Me., affirmed in 16 A. B. R. 303, 144 Fed. 392): "The referee has found affirmatively that the bankrupt has under her control the balance of the fund to the amount of \$2,425, and that she had possession or control of it at the date of the filing of the petition bankruptcy; that she has withheld and concealed the same from her trustee, and is now withholding and concealing the same from him. The referee had the witness before him. He conducted the examination of the bankrupt herself, saw her appearance, and was a proper tribunal to decide the questions of fact submitted to him. After full examination of the testimony, I cannot say that I should have come to a different conclusion. In any event the conclu-

⁸¹ In *re Jackier*, 24 A. B. R. 790, 179 Fed. 720 (D. C. Pa.).

⁸² In *re Baum*, 22 A. B. R. 295, 169 Fed. 410 (C. C. A. Ark.).

⁸³ In *re Tudor*, 2 A. B. R. 808, 96 Fed. 942 (D. C. Colo.). Compare, post, § 2861.

The subsequent contempt proceedings to punish for failure to comply with the order of surrender may not be converted into a review of the order itself. See post, § 1857.

sion of a competent referee, who has seen the witnesses, is entitled to great weight."

But see, *contra*, *In re Mayer*, 3 A. B. R. 533, 98 Fed. 839 (D. C. Wis.): "On review of the order in such case, I am of opinion that the ordinary rule as to the force of the findings of fact is not applicable, for the reason that determination is not governed by the weight of testimony. Enforcement of the order devolves upon the reviewing court, and with it the duty to ascertain that cause exists, beyond reasonable doubt, for the exercise of the severe means thus intrusted to the court, where an error in judgment as to the credibility or force of testimony involves indeterminate imprisonment without just cause. Let this opinion be certified to the referee for modification of the order in accordance therewith, and further proceedings thereupon as advised."

Nor will the Circuit Court of Appeals set aside the District Court's order affirming the referee's summary order except for manifest error.

In re Cole, 16 A. B. R. 303, 144 Fed. 392 (C. C. A. Me., affirming 14 A. B. R. 389): "The question whether the money was in the possession or control of Mrs. Cole is, under the circumstances of this case, what the law designates a question of fact, over which we could, of course, have no jurisdiction on this petition, which raises only questions of law, unless the finding of the District Court against her was so wholly unjustified on the proofs as would require us, on a writ of error, to set aside a verdict of the jury for want of any evidence whatever to sustain it, or for some other reason kindred thereto."

In re Levy & Co., 15 A. B. R. 166, 142 Fed. 443 (C. C. A.): "The referee has ruled, and the court has affirmed his ruling, that this failure of the petitioner to account sufficiently establishes that the goods are still in his possession. If it be assumed that there might otherwise have been a question as to the correctness of the view taken by the court, yet, as its order is based on the finding of the referee on all the evidence that the bankrupts have the property or its value in their possession, this order should not be reversed except upon clear proof of error."

And where the record, upon a petition to revise an order that a bankrupt pay into court a certain amount in cash, does not contain the evidence taken before the referee, it will be presumed that the facts were sufficient to sustain his finding and order, and only matters of law, apparent upon the face of the record, may be considered.⁸⁴

Likewise, where an order requires a bankrupt to pay over money, it will be presumed that such assets consisted of money in his possession and under his control at the time the order was made, and that he was able to comply with the order.⁸⁵

§ 1855. Whether "Review" or "Appeal."—Summary orders upon bankrupts and others to surrender assets are reviewable by the Circuit Court of Appeals only under § 24 (b);⁸⁶ and, at any rate as to others than bank-

⁸⁴. *In re Baum*, 22 A. B. R. 295, 169 Fed. 410 (C. C. A. Ark.).

⁸⁵. *In re Baum*, 22 A. B. R. 295, 169 Fed. 410 (C. C. A. Ark.), quoted at § 1845.

⁸⁶. See general subject of "Appeals and Errors," post, § 2938. *Schweer v. Brown*, 12 A. B. R. 673, 195 U. S. 171. Compare, *In re Rosser*, 4 A. B. R. 153, 101 Fed. 562 (C. C. A. Mo.).

rupts, only by writ of error or petition to revise, not by appeal.⁸⁷

§ 1856. Contempt for Disobedience of Summary Orders.—If the bankrupt or such other party thus found to have assets of the estate in his control and ordered to surrender the same, fails or refuses to surrender them, he may be punished for contempt.⁸⁸

Trust Co. v. Wallis, 11 A. B. R. 363, 126 Fed. 464 (C. C. A. Penn.): "For disobedience of such order, the court in bankruptcy undoubtedly has the power, by attachment for contempt, to enforce compliance with such order, and punish refusal to comply."

Obiter, *In re Rosser*, 4 A. B. R. 153, 101 Fed. 562 (C. C. A. Mo.): "The power of a court to punish for contempt of its proceedings, for disobedience of its lawful orders, is inherent in the being of every court of general jurisdiction. Without it the orders of a court would be without force or effect, would command neither respect nor obedience, and there would be neither warrant nor reason for its longer existence. From the earliest annals of our law this power has been exercised. It rests upon the fundamental principles of judicial establishments, and is inseparable from the existence, as well as from the usefulness, of a court of general jurisdiction."

^{87.} *In re D. Abraham* (Bernheimer *v. Bryan*), 2 A. B. R. 266, 93 Fed. 767 (C. C. A. Ala., reversed, on other grounds, in *Bryan v. Bernheimer*, 5 A. B. R. 623, 181 U. S. 188); *Bank v. Title & Trust Co.*, 14 A. B. R. 102, 198 U. S. 288; *Schweer v. Brown*, 12 A. B. R. 673, 195 U. S. 171; *In re Mertens*, 15 A. B. R. 702, 142 Fed. 445 (C. C. A. N. Y.); *Samel v. Dodd*, 16 A. B. R. 165, 142 Fed. 68 (C. C. A. Ga.). Instance, *In re Cole*, 16 A. B. R. 303, 144 Fed. 392 (C. C. A. Me.). Compare, *In re Cole*, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.).

Apparently *contra*, *obiter*, where questions of fact presented, *Ellis v. Krulewitch*, 15 A. B. R. 615, 141 Fed. 954 (C. C. A.): "It is difficult to perceive how error of law could be predicated of it, because it is made upon evidence from which men of different minds might draw different conclusions, and a question of this nature is a question of fact, reviewable by appeal and not by error."

Modification of referee's order. *In re Hershkowitz*, 14 A. B. R. 86, 136 Fed. 950 (D. C. N. Y.).

^{88.} *Samel v. Dodd*, 16 A. B. R. 166, 142 Fed. 68 (C. C. A. Ga.); *In re DeGottardi*, 7 A. B. R. 728, 114 Fed. 328 (D. C. Calif.); *In re Wilson*, 8 A. B. R. 612, 116 Fed. 419 (D. C. Ark.); *In re Purvine*, 2 A. B. R. 787, 96 Fed. 192 (C. C. A. Tex.); *In re Henderson*, 13 A. B. R. 782 (D. C. Penn.); *In re Deuell*, 4 A. B. R. 60, 100 Fed. 633 (D. C. Mo.); *In re Alphin & Lake Cotton Co.*, 14 A. B. R. 194, 134 Fed. 477 (D. C. Ark.);

In re Gerstel, 10 A. B. R. 413, 123 Fed. 166 (D. C. Ills.); *Ripon Knitting Wks. v. Schreiber*, 4 A. B. R. 299, 101 Fed. 810 (D. C. Wash., affirmed, on review, in 104 Fed. 1006); (1867) *In re Salkey*, 11 N. B. Reg. 423, Fed. Cases, No. 12,253; *In re Anderson*, 4 A. B. R. 640, 103 Fed. 854 (D. C. S. C.); *In re Schlesinger*, 4 A. B. R. 361, 102 Fed. 117 (C. C. A. N. Y., affirming 3 A. B. R. 342, 97 Fed. 930); *In re Levy & Co.*, 15 A. B. R. 166, 142 Fed. 442 (C. C. A.); *In re Schachter*, 9 A. B. R. 499 (D. C. Ga.); *In re Mayer*, 3 A. B. R. 534, 101 Fed. 695 (D. C. Wis.); *Moody v. Cole*, 17 A. B. R. 818 (D. C. Me.); *In re Grassler & Reichwald*, 18 A. B. R. 694, 154 Fed. 478 (C. C. A. Calif.); *In re Lasky*, 20 A. B. R. 729, 163 Fed. 99 (D. C. Ala.); *obiter* (present possession not sufficiently proved), *In re Cole*, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.); *In re Holland*, 23 A. B. R. 835, 176 Fed. 624 (D. C. N. Y.), quoted, on other points, § 1840; *In re Marks*, 23 A. B. R. 911, 176 Fed. 1018 (D. C. Pa.), quoted at §§ 1843, 1857; *obiter*, *In re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.); instance, *In re Richards*, 25 A. B. R. 176, 183 Fed. 501 (D. C. Ark.); *In re Meier*, 25 A. B. R. 272, 182 Fed. 799 (C. C. A. Mo.).

General order to surrender all assets, books, etc., contained in order of appointment of receiver, whether sufficient to predicate contempt, *Skubinsky v. Bodek*, 22 A. B. R. 699, 172 Fed. 340 (C. C. A. Pa.); also, see ante, § 392, note.

In *re Grassler & Reichwald*, 18 A. B. R. 694, 154 Fed. 478 (C. C. A. Calif.): "And if the referee could lawfully make the order, it follows that the court below could deal with the petitioner (on review) as for contempt, and commit him to imprisonment for refusal to obey the order."

In *re McCormick*, 3 A. B. R. 340, 97 Fed. 566 (D. C. N. Y.): "There can be no doubt of the authority of the court to enforce obedience to all 'lawful orders' and to punish contempts by virtue of the provisions above referred to. As such punishment may involve imprisonment, however, this power should be cautiously exercised, and in cases only where willful disobedience by the bankrupt is proved beyond reasonable doubt, as in a criminal case."

The court may proceed either under the general power of all courts to punish contempt^{88a} as restricted by the provisions of the Federal Statute, U. S. Rev. Stat., § 725, specifying contempts in federal courts,^{88b} or under the specific provisions of the Bankruptcy Act, § 2 (13) for enforcing obedience to lawful orders, and § 2 (16) to punish contempts committed before referees.^{88c}

Punishment for contempt for failure to surrender property when ordered to do so is not the exercise of any new function in a court of equity.⁸⁹

An officer of a state court may be punished for such contempt,⁹⁰ but that he was acting under advice of counsel may excuse him.⁹¹ Advice of counsel will not excuse the failure of a petitioning creditor, to whom under claim of ownership a receiver in bankruptcy had surrendered certain property, to return the property where, later, it was judicially determined that the petitioner, under mistaken advice of counsel, had waived his claim as mortgagee (counsel considering it void for lack of proper record), and had assumed the sole position of a creditor.⁹²

§ 1857. Whether Evidence on Which Order for Surrender Based May Be Re-Examined.—On principle it would seem that, since the order to surrender assets may be granted only on convincing evidence or evidence beyond a reasonable doubt, the court, on contempt proceedings for failure

^{88a}. Compare post, § 2330 "Contempt, What Constitutes, in General;" also see *In re Cole*, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.).

^{88b}. Compare post, § 2330; also see *Boyd v. Glucklich*, 8 A. B. R. 398, 116 Fed. 131 (C. C. A. Pa.); *In re Probst*, 30 A. B. R. 600, 205 Fed. 512 (C. C. A. N. Y.).

^{88c}. *In re Cole*, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.).

⁸⁹. See ante, § 1883 [1833].

⁹⁰. *In re Geiser*, 12 A. B. R. 208 (D. C. Mont.).

⁹¹. As to practice in citations for contempt for failure to surrender: See post, §§ 2330, 2341, also see *In re Purvine*, 2 A. B. R. 787, 96 Fed. 192 (C. C. A. Tex.); *In re McCormick*, 3 A. B. R.

340, 97 Fed. 566 (D. C. N. Y.); *Ripon Knitting Wks. v. Schreiber*, 4 A. B. R. 299, 101 Fed. 810 (D. C. Wash.); *Boyd v. Glucklich*, 8 A. B. R. 398 (C. C. A. Iowa). *In re Geiser*, 12 A. B. R. 208 (D. C. Mont.); *In re Cole*, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.).

Proceedings for contempt for failure to surrender assets dismissed without prejudice to later renewal where bankrupt under indictment for embezzlement of same funds, *In re Smelting Co.*, 17 A. B. R. 141 (D. C. Penn.).

⁹¹. *Orr v. Tribble*, 19 A. B. R. 849, 158 Fed. 897 (D. C. Ga.); also see post, § 2333; and ante, § 1474, note.

⁹². *In re Strobel*, 20 A. B. R. 754, 163 Fed. 380 (D. C. N. Y.).

to obey such order, ought not to go behind the order itself, if the order was not appealed from, and ought to take into consideration only facts arising subsequently thereto, leaving the propriety of the order itself remediable by appeal or petition for review, since otherwise the contempt proceedings would be diverted into an appeal from the order of surrender itself.⁹³

In *re Lans*, 19 A. B. R. 458, 158 Fed. 610 (C. C. A. N. Y.): "Having failed to secure a review of the order of December 14th, 1906, which found that the bankrupt was concealing property and directed him to turn it over to the trustee, he is in no position to question its propriety upon this petition which brings up only the order adjudging him to be in contempt for failure to comply with the provisions of said order of December 14th."

In *re Haring*, 29 A. B. R. 387, 193 Fed. 168 (C. C. A. Mich.): "It appears both by the referee's findings and the court's opinion that the referee's statement of the account was in several material respects but an approximation; the findings do not purport to be based solely upon book entries or other controlling data. Surely it was quite as open to the judge, as it was to the referee, to draw inferences and deduce a conclusion from such a source as this. It was not even a case of conflicting evidence, depending upon the credibility of witnesses who were before the referee and not the court. *Ohio Valley Bank Co. v. Mack* (C. C. A., 6th Cir.), 20 Am. B. R. 40, 163 Fed. 155, 158, 89 C. C. A. 605; In *re Swift* (D. C. Mass.), 9 Am. B. R. 237, 118 Fed. 348, 349; 1 *Loveland on Bankruptcy*, 4th ed., pp. 225, 226. The court, not the referee, was charged with the responsibility of exercising the power of commitment for contempt (*Smith v. Belford* (C. C. A., 6th Cir.), 5 Am. B. R. 291, 106 Fed. 658, 661); and it will not do to say that findings like these operate (if indeed findings of the referee can ever operate) as an estoppel upon the bankrupt court or otherwise conclude it."

Compare, In *re Haring*, 27 A. B. R. 285, 193 Fed. 168 (D. C. Mich.): "There are two distinct lines of decision upon this subject founded upon different and divergent theories and conceptions of the law. In one line are the courts which hold in substance that an order of the referee, made after a hearing and supported by evidence, adjudging the bankrupt to have in his possession and control a certain sum of money or specific property belonging to his estate and requiring him to turn over to the trustee such money or property, which order he neither obeys nor seeks to have reviewed, creates a presumption of the ability of the bankrupt to comply with the order and casts upon him the burden of proving the contrary; and that such presumption becomes final and conclusive unless the bankrupt gives an adequate explanation of what has become of the money or property.

"In the other line are the courts which hold in substance that in proceedings against a bankrupt for contempt for failure to obey an order of the referee requiring him to turn over money or property to the trustee, such order may be referred to and given the weight to which it is entitled under all the circumstances, but the court should make a new and independent investigation and should consider all material evidence relating to what preceded as well as what followed the referee's report and, from such investigation and from such evidence, determine whether or not the order of the referee was justified, whether or not the bankrupt's disobedience thereof is willful and contumacious and whether or not the bankrupt has the present ability to comply therewith."

In *re Home Discount Co.*, 17 A. B. R. 175, 147 Fed. 538 (D. C. Ala.): "He

93. In *re Frankel*, 25 A. B. R. 920, 184 Fed. 539 (D. C. N. Y.).

cannot ignore the order until the referee under § 14 certifies his disobedience to the judge, and then bring forward again, in his defense, matter contested before the referee prior to the making of the order, provided the order itself be not void. The method of correcting error is by appeal, and not by disobedience."

However some decisions that touch upon the point, although not directly deciding the proposition, seem to indicate that on contempt proceedings the evidence on which the original order was based may be re-examined.⁹⁴

At any rate, the order for surrender makes a *prima facie* case of possession, such that the trustee's petition for punishment for contempt need not allege ability to comply with the original order for surrender.

In *re Stavrahn*, 23 A. B. R. 168, 174 Fed. 330 (C. C. A. N. Y.): "We do not find in the statute, the General Orders or in any decision which has been called to our attention any authority for the proposition that the petition should contain an affirmative allegation of the bankrupt's present ability to comply with the order requiring him to turn over property. That is more properly a matter of defense. When the moving papers indicate that it has been determined after a full hearing that the bankrupt has concealed some specific piece of property; that he has been ordered to turn it over to the trustee; that he has been duly served with such order, and that he has failed to comply with such order; sufficient is charged to put him upon his defense. Of course he should have notice of the motion to punish him for such disobedience and have his 'day in court' when he may present what he may have to urge against such motion and an opportunity to be heard. All these the petitioner had in this case. * * * When the matter was before the District Court in February, 1909, on the final application to punish the bankrupt for a wilful and contumacious disobedience of the order of August 5, 1908, directing him to pay over, it appeared that before the last-named order was made there had

94. In *re Davidson*, 16 A. B. R. 339 (D. C. R. I.); In *re Rosser*, 4 A. B. R. 153, 101 Fed. 562 (C. C. A. Mo.); *Samel v. Dodd*, 16 A. B. R. 166, 142 Fed. 68 (C. C. A. Ga.); In *re Davidson*, 16 A. B. R. 339 (D. C. R. I.); In *re Anderson*, 4 A. B. R. 641, 103 Fed. 854 (D. C. S. C., reversed, on other grounds, sub nom. *McGahan v. Anderson*, 7 A. B. R. 641, 113 Fed. 115); compare, In *re Cole*, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.); *Samel v. Dodd*, 16 A. B. R. 166, 142 Fed. 68 (C. C. A. Ga., distinguished in In *re Stavrahn*, 23 A. B. R. 168, 174 Fed. 330, C. C. A. N. Y.). Compare, In *re Eddleman*, 19 A. B. R. 45, 154 Fed. 160 (D. C. Ky.); instance, In *re Lasky*, 20 A. B. R. 729, 163 Fed. 99 (D. C. Ala.); In *re Rogowski*, 21 A. B. R. 553, 166 Fed. 165 (D. C. Ga.), quoted at § 1845; In *re Goodrich*, 25 A. B. R. 787, 184 Fed. 5 (C. C. A. Mass.); *Stuart v. Reynolds*, 29 A. B. R. 412, 204 Fed. 709 (C. C. A. Ala.), quoted at §§ 1841, 1843, 1845; compare, In *re Epstein*, 30 A. B. R. 387, 206 Fed. 568 (D. C. Pa.); instance, In *re Banzai Mfg.*

Co., 25 A. B. R. 497, 183 Fed. 298 (C. C. A. N. Y.); instance, In *re Richards*, 25 A. B. R. 176, 183 Fed. 501 (D. C. Ark.).

Proceedings for Contempt Different from Order of Surrender.—A proceeding for contempt is of a different character from one for surrender of property; In *re Davidson*, 16 A. B. R. 338, 143 Fed. 673 (D. C. R. I.); In *re Cole*, 16 A. B. R. 302, 144 Fed. 392 (C. C. A. Me.).

Review of Summary Order Treated as if on Contempt for Disobedience.—Since the evidence to support the order should be of equal weight with that for contempt one court considered a review as if it were a contempt proceedings. In *re (Wolfe) Adler*, 21 A. B. R. 371, 170 Fed. 634 (D. C. Okla.).

Compare *obiter* (imprisonment ordered though plea of inability to pay held admissible, it not appearing, however, whether or not the inability arose subsequently). In *re Cummings*, 26 A. B. R. 130, 186 Fed. 1020 (D. C. Pa.).

been two adjudications, after full hearings, whereat the bankrupt testified and had the right to produce witnesses, both finding that the bankrupt had fraudulently concealed at least \$5,000, the profits of a certain real estate transaction which he should have turned over with the rest of his estate. It further appeared that the bankrupt had not taken any steps to review either of these adjudications. Certainly this was sufficient, *prima facie*, to establish the proposition that at some time subsequent to the bankruptcy, and prior to August 5, 1908, he was in the actual possession of that particular sum of money. In the face of such a finding it was incumbent on the bankrupt to give some reasonable explanation as to why it was that he did not turn it over in compliance with the order requiring him so to do; it was for him to explain how and why it was that this particular sum, in his possession a few months before, had disappeared, so that he no longer 'had the ability to turn it over in compliance with the order.' This he wholly failed to do."

Also, compare, *In re Marks*, 23 A. B. R. 911, 176 Fed. 1018 (D. C. Pa.): "In this proceeding the court will not re-examine the question whether the order should ever have been made—either at all, or in the particular amount fixed by the referee. The trustee has therefore an unimpeachable right to the money specified in the order, and presumatively the bankrupt is able to pay it; but the admission must nevertheless be made, that the presumption may not correspond with the fact, and that in reality the bankrupt cannot comply with the order. Unless he has the physical ability to comply, he should not be committed for contempt; in practical effect, although perhaps not in legal contemplation, this would revive the abolished penalty of imprisonment for debt. If he cannot pay, and if his inability is the result of his own criminal act, he may of course be punished by the criminal law, although no civil remedy may be available in the situation. Even if he has misappropriated the money, the court has not the power to imprison him in a proceeding for contempt; for this would deprive him of his constitutional right to submit the charge of misappropriation to a jury in the proper criminal court, would deprive him also of the inseparable right to be exempt from imprisonment for such an offense until he shall have been lawfully convicted. And it is also true that he cannot be imprisoned in a proceeding for contempt, if for any other reason he cannot produce the money; for the court cannot imprison as a punishment, it can only imprison to compel obedience to its order. But with an order to pay in force against him, and with the need to overcome the presumption of his ability to comply, it will no doubt happen at times that a bankrupt may fail to meet the burden of proof, and may be obliged to go to jail until he satisfies the court that he was telling the truth when he pleaded poverty." Also quoted at § 1843.

§ 1858. Opportunity Must Be Given to Defend on Contempt.—

But the bankrupt or such other party should not be punished for contempt because of his failure to comply with the order of the court, before he is given an opportunity to prove his inability to do so.⁹⁵

In re Hausman, 10 A. B. R. 64, 121 Fed. 984 (C. C. A. N. Y.): "In affirming the order of the court below, we do not consider the question whether the

⁹⁵ *Boyd v. Glucklich*, 8 A. B. R. 398 (C. C. A. Iowa); *In re Davidson*, 16 A. B. R. 338, 143 Fed. 673 (D. C. R. I.); *In re Cole*, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.); *obiter*, *In re Stavrah*, 23 A. B. R. 168, 174 Fed. 330 (C. C. A. N. Y.), quoted *ante*, § 1857; *In re Banzai Mfg. Co.*, 25 A. B. R. 497,

183 Fed. 298 (C. C. A. N. Y.); *In re Frankel*, 25 A. B. R. 920, 184 Fed. 539 (D. C. N. Y.); *Stuart v. Reynolds*, 29 A. B. R. 412, 204 Fed. 709 (C. C. A. Ala.), quoted at §§ 1841, 1843, 1845; *instance*, *In re Richards*, 25 A. B. R. 176, 183 Fed. 501 (D. C. Ark.).

bankrupt should be punished for contempt in the event of failing to comply with the order, as that question, although the one principally argued, is not here. If it should be sought to punish him for contempt the court below will doubtless give him an opportunity to prove his inability to comply with the order."

In *re Cole*, 16 A. B. R. 304, 144 Fed. 392 (C. C. A. Me., reversing, on this point, 14 A. B. R. 389): "We think, however, that there was error in that the District Court entered in substance a judgment for contempt, accompanying an alternative order for committal. It is plain that a proceeding for contempt is of a different character from one resulting in a mere order for the payment of money to a trustee in bankruptcy. It is claimed that it is criminal in its nature, while an order for the mere payment of money is purely civil; that it would be justified only by the proofs and the amount of proofs requisite on ordinary criminal issues; and that it is in effect an independent proceeding which can be initiated only after an order for payment of money has been disobeyed, and an order to show cause, or some other new notice, given to the person alleged to be in default. It is sufficient now to say that the record does not show that Mrs. Cole had any day in court on the issue involved in that part of the order in question. Without undertaking to say in what manner an issue may be so presented as to justify a proceeding for an alleged contempt, and entering a penal judgment on account thereof, we are of the opinion that the record should show that the issue had been made in some way, and that the person adjudged guilty of contempt had had an opportunity to be heard in reference thereto. *Rapalje on Contempts* (1887), 126, 127, 128. For this reason, the order to which this petition relates must be annulled, except only so far as it affirms the decision of the referee which directed that the money in question should be paid to the trustee."

A petition should be filed⁹⁶ and it should allege that the noncompliance with the order was wilful.⁹⁷ And due notice must be given.⁹⁸

A referee should not make a certificate of contempt, without such hearing and notice,⁹⁹ except where it consists of an affront in open court and the referee initiates the proceedings.¹

§ 1859. Evidence on Contempt to Be beyond Reasonable Doubt.—And the evidence of ability to comply with the order must appear beyond reasonable doubt;² or, at any rate, must be clear and con-

96. In *re Cole*, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.).

97. In *re Cole*, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.). But compare, distinction made, In *re Stavrah*, 23 A. B. R. 168, 174 Fed. 330 (C. C. A. N. Y.).

98. In *re Smelting Co.*, 15 A. B. R. 834 (D. C. Penn.). Obiter, In *re Stavrah*, 23 A. B. R. 168, 174 Fed. 330 (C. C. A. N. Y.), quoted ante, § 1857.

99. See post, § 2337½. See, also, *Magen & Magen*, 24 A. B. R. 63, 179 Fed. 572 (D. C. Pa.).

1. See post, § 2337. Also, see, *Magen & Magen*, 24 A. B. R. 63, 179 Fed. 572 (D. C. Pa.).

2. In *re Anderson*, 4 A. B. R. 641, 103 Fed. 854 (D. C. S. C., reversed on other grounds, sub nom. *McGahan v. Anderson*, 7 A. B. R. 641, 113 Fed. 115

C. C. A.); In *re Mayer*, 3 A. B. R. 534, 98 Fed. 839 (D. C. Wis.); In *re Goldfarb Bros.*, 12 A. B. R. 386 (D. C. Ga.); *Moody v. Cole*, 17 A. B. R. 818 (D. C. Me.). But compare, inferentially contra, In *re Feller*, 17 A. B. R. 787, 149 Fed. 244 (D. C. N. Y.); In *re Levy & Co.*, 15 A. B. R. 169, 142 Fed. 442 (C. C. A.); In *re Mize*, 22 A. B. R. 577, 172 Fed. 945 (D. C. Ala.). Compare, In *re Cole*, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.); also, compare, In *re (Wolfe) Adler*, 21 A. B. R. 371, 170 Fed. 634 (D. C. Okla.); *Stuart v. Reynolds*, 29 A. B. R. 412, 204 Fed. 709 (C. C. A. Ala.), quoted at §§ 1841, 1843, 1845. See also, cases cited under similar propositions as to orders for surrender, ante, § 1842. See post, § 2340.

As to Whether Imprisonment for

vincing.³

Kirsner v. Taliaferro, 29 A. B. R. 832, 202 Fed. 51 (C. C. A. Va.): "We know no better way of stating the quantum of proof which should be insisted on than to say, as other courts have said, that it should be sufficient to establish the fact beyond reasonable doubt. Such a rule is required, not only for the protection of the liberty of the citizen, but for the preservation of the dignity of the court itself. It is not well that there should be many occasions in which, after sending a man to jail for refusing to obey an order, the court will feel constrained to release him without the order being obeyed. Unless the power of commitment as a means of compulsion is exercised only when there is no real question of the ability of the defendant to do what he is commanded, such an outcome will not be uncommon."

Stuart v. Reynolds, 29 A. B. R. 412, 204 Fed. 709 (C. C. A. Ala.): "In contempt cases, and especially in those which involve the charge of another criminal offence besides the contempt, the rules of evidence applicable to civil cases in reference to presumptions and the shifting of the burden of proof, do not apply; but the proceedings and the rules of evidence and presumptions of law applied in criminal cases should be observed. * * * The numerous recent cases that hold that the guilt of an accused charged with contempt must be proved, not by a preponderance of evidence, but beyond a reasonable doubt, show an application of the rules of evidence as they are applied in criminal cases."

In re Cole, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.): "* * * and while also it seems to be conceded on all sides that, before committing for contempt, the court should be satisfied beyond a reasonable doubt of a wilful refusal or a wilful act on the part of the person proceeded against yet neither the sixth amendment to the Constitution, nor any principle shadowed out by it, has strict application to proceedings of the character before us."

In re Switzer, 15 A. B. R. 470, 140 Fed. 976 (D. C. S. Car.): "The court, in making an order to commit a bankrupt to jail as for contempt for failure to account for goods and money, should be governed by the same considerations which would influence a jury in a criminal prosecution, giving to the bankrupt the benefit of any reasonable doubt."

In re Davidson, 16 A. B. R. 339, 143 Fed. 673 (D. C. R. I.): "The authorities seem to be agreed that no contempt order should be made unless the court is satisfied of the present ability of the bankrupt to comply with the decree for the payment of money. While the admitted receipt of goods or money, and repeated refusals to explain or account for their disappearance, may lead to a belief in a present possession or control, and be a sufficient basis for a contempt order (*In re Levy & Co.*, 15 A. B. R. 166, 142 Fed. 442), yet it does not seem to me that the question of the present ability of a bankrupt to comply with an order should be determined upon an artificial rule of proof to be applied irrespective of the circumstances of the particular case.

Contempt for Failure to Obey Order to Surrender Assets, Criminal Proceedings.—As to whether imprisonment for contempt for disobedience of an order to surrender assets is a criminal proceedings, see ante, § 1842.

Force and weight of sworn denial: *Moody v. Cole*, 17 A. B. R. 818 (D. C. Me.). See also, similar proposition under "Summary Order to Surrender," ante, §§ 1843 and 1844.

Compare, where court says the bankrupt's bare denial of present ability does not satisfy him, *In re Cummings*, 26 A. B. R. 130, 186 Fed. 1020 (D. C. Pa.).

3. *In re Haring*, 27 A. B. R. 285, 193 Fed. 168 (D. C. Mich.); *In re Haring*, 29 A. B. R. 387, 193 Fed. 168 (C. C. A. Mich.).

"That a person has been guilty of fraudulent appropriation of property, and has concealed it by falsehood or perjury, does not always lead to the belief that the failure to make restitution upon an order is contumacious and wilful. Where the amount concealed is small, and such as might readily have been spent, or where the circumstances are such as to indicate that the bankrupt was merely the person in nominal control of the business, and merely the instrument of others in a scheme for defrauding creditors, it is quite reasonable, under such circumstances, to believe even a person who has been guilty of fraudulent appropriation, and of fraudulent statements, when she swears that she has not now the fruits of the fraud, nor any control over them. * * *

"If, having doubts of her present ability to pay, I should commit this bankrupt to confinement in jail upon a conjecture that her husband or other persons, actual principals in the fraud, may come to her relief with a sum of money equal to that which she has been ordered to pay over, I should, in my opinion, be abusing the power to punish for contempt. Creditors who sell to persons of doubtful or unknown financial standing, and of unknown or suspicious character for integrity, and who, by their own lack of ordinary diligence, have become the victims of fraud, should proceed for redress under the ordinary methods of legal procedure, and cannot expect to use, as an ordinary agent in the collection of debts, the power to imprison for contempt, which is to be applied only in cases of contumacious resistance to the orders of court. While there is no doubt of the power of the court to enforce its order for the surrender of property or money, when clearly satisfied that it is within the power of the bankrupt or other person to comply with such order, I am not so satisfied in this case."

And ability to comply with the order and wilful disobedience of it are essential.⁴ But the contempt proceedings are not criminal proceedings, and it is not forbidden to introduce the bankrupt's schedules nor his general examination against him, as would be the case were the proceedings criminal.⁵

§ 1859½. Whether "Petition for Revision" or "Writ of Error" to Review Contempt Proceedings.—The court, as above remarked (§ 1856), may proceed either under the general power of all courts to punish contempts as the same is modified by U. S. Rev. Stat., § 725, or under the specific provisions of Bankruptcy Act, § 2 (13) and (16); and the method of review, as in other cases, depends on whether it is "a proceedings in bankruptcy," or a "controversy arising in a bankruptcy proceedings." Thus, an order of the bankruptcy court committing the bankrupt to prison until he shall surrender to his trustee property of the estate in his control, is an order made in the progress of the bankruptcy proceedings with a view to the obtaining of the possession of the property of the estate or to enforce performance of an order of the court, and the proper procedure therefore would be to bring the matter before the Circuit Court of Appeals by a petition to revise. On the other hand, where the proceedings to punish for contempt are instituted to punish an act already committed and not for enforcing in the future the prompt administration of

4. In re Purvine, 2 A. B. R. 787, 96 Fed. 192 (C. C. A. Tex.). Also, compare, analogously, ante, § 1845, et seq.

5. Compare, suggestively, In re Cole, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.).

the estate, as, for instance, to punish the violation of an injunction, is an entirely different and distinct proceedings, and is reviewable by "writ of error" as a "controversy arising in bankruptcy proceedings."^{5a}

Kirsner v. Taliaferro, 29 A. B. R. 832, 202 Fed. 51 (C. C. A. Va.): "The questions as to when in contempt proceedings an appeal will lie and when a petition for revision is the proper proceeding, has been discussed by the Circuit Court of Appeals of the Ninth Circuit. *Morehouse v. Pacific Hardware & Steel Co.*, 24 A. B. R. 178, 177 Fed. 337 (C. C. A. Nev.). In that case certain persons had been enjoined by the court of bankruptcy from prosecuting a suit in a state court. They had violated the injunction. It was sought to have them punished for contempt in the bankruptcy court. They brought the matter to the Circuit Court of Appeals by a petition to 'revise. In dismissing it, the court said that the order complained of 'was not made with a view to obtain possession of the property of the bankrupt or to enforce a prior order of the court, but it is a criminal proceeding to punish by fine or imprisonment those who have been guilty of violating an injunction of the court.' The opinion had previously declared that 'proceedings in bankruptcy' include among other things, 'orders requiring the bankrupt to surrender property of the estate in bankruptcy and orders requiring the bankrupt's voluntary assignee to surrender property of the estate.' 'These are questions which with a view to the prompt administration and distribution of the assets of the bankrupt the law permits to be summarily disposed of by revision.'

"We are therefore of opinion, as well upon reason as upon authority, that an order of the court of bankruptcy ordering the bankrupt to turn over to his trustees property of the estate and committing him to prison until he does so is an order made in a proceeding in bankruptcy and may be brought before the Circuit Court of Appeals by a petition to superintend and revise in matter of law under § 24b."

In re *Cole*, 20 A. B. R. 761, 163 Fed. 180 (C. C. A. Me.): "If the proceeding in the District Court was taken by virtue of the specific provision of the statute, it would be the natural presumption that the proper method of reaching us would be that which was in fact availed of, namely, a petition for revision under the same act. If, on the other hand, the proceeding in the District Court had relation to the general powers vested in superior courts of judicature with reference to contempts, the question would at once arise whether the present petitioner, Mrs. Cole, should not have come to us by writ of error."

§ 1860. Procedure on Obtaining Surrender from Court Officers.

—Where surrender from a court officer is sought, either the trustee makes direct application to the court whose officer has the custody, for a summary order upon the officer to surrender the assets; or he applies to the bankruptcy court itself therefor, the comity of courts prescribing that the latter method be not resorted to until efforts have reasonably been exhausted to get the order from the court already in charge of the property.⁶

5a. Compare post, § 2879¼, "Contempt Proceedings;" also, § 2330½, "Distinction between Civil and Criminal Contempt."

6. See "Procedure on Annuling of Liens Obtained by Legal Proceed-

ings," § 1471, et seq. See summary orders on "Assignees and Receivers," ante, § 1827 and § 1830, et seq. See ante, "Comity Requires Resort First to State Tribunal," § 1637.

Advice of counsel protects state re-

But the requirement that application should first be made to the state court where the proceedings are pending, does not prevail where an emergency exists; and the bankruptcy court in such case has the right to proceed at once by direct order upon the court officer.

§ 1861. If Application Be to State Court Whose Officer in Control, Procedure Follows That of Such Court.—If the application be made to the state court whose officer is in control of the property sought for, the procedure, of course, follows that of the state court.

§ 1862. If Application Be to Bankruptcy Court, Procedure Follows Ordinary Rules as to Summary Orders on Bankrupts and Agents.—If the application be made in the bankruptcy court, however, for the order of surrender upon the state court's officer, it follows the ordinary rules as to summary orders on bankrupts and others.

§ 1863. Jurisdiction to Determine Facts Requisite to Summary Jurisdiction.—The bankruptcy court has jurisdiction in the summary proceedings to determine the existence of the facts requisite to give it the jurisdiction thus to proceed summarily.⁷

Mueller v. Nugent, 184 U. S. 15, 7 A. B. R. 224: "But suppose that respondent had asserted that he had the right to possession by reason of a claim adverse to

ceiver, who has at one time voluntarily surrendered possession to the bankruptcy receiver without leave of the state court, and thereafter has retaken possession without leave of the federal court, and he will not be punished for contempt. In re Watts, 10 A. B. R. 113, 190 U. S. 1.

Before applying to the state court, the trustee should first get authority from the bankruptcy court, *Bear v. Chase*, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S. C.); such authority may require the trustee to make a limited request, *Bear v. Chase*, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S. C.).

Voluntary surrender by state receiver without first obtaining order permitting, In re Watts, 10 A. B. R. 113, 190 U. S. 1.

And application to the state court first is not such an election of forum as to debar the bankruptcy court from subsequently issuing its restraining order. *Bear v. Chase*, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S. C.).

7. In re Breslauer, 10 A. B. R. 33, 121 Fed. 910 (D. C. N. Y.); In re Weininger, Bergman & Co., 11 A. B. R. 424, 126 Fed. 875 (D. C. N. Y.); *Mueller v. Nugent*, 7 A. B. R. 224, 184 U. S. 1; In re Davis, 9 A. B. R. 675 (D. C. Tex.); In re Andre, 13 A. B. R. 132 (C. C. A. N. Y.); In re Teschmacher & Mrazay, 11 A. B. R. 547, 127 Fed. 728 (D. C. Penn.); In re Muncie Pulp Co., 14 A.

B. R. 73, 139 Fed. 546 (C. C. A. N. Y.); *Louisville Trust Co. v. Comingor*, 7 A. B. R. 421, 184 U. S. 18; In re Tune, 8 A. B. R. 285, 115 Fed. 906 (D. C. Ala.); inferentially, In re Adams, 12 A. B. R. 367, 130 Fed. 788 (D. C. R. I.); *Schweer v. Brown*, 12 A. B. R. 673, 195 U. S. 171; obiter, In re Waukesha Water Co., 8 A. B. R. 715, 116 Fed. 1009 (D. C. Wis.); obiter, In re Milk Co., 16 A. B. R. 732 (D. C. Penn.); obiter, impliedly, In re Sunseri, 18 A. B. R. 235 (D. C. Penn.); *Knapp & Spencer v. Drew*, 20 A. B. R. 355, 160 Fed. 413 (C. C. A. Neb.), quoted at § 1800; In re Hayden, 22 A. B. R. 764, 172 Fed. 623 (D. C. Mass.); In re Horgan, 21 A. B. R. 31, 164 Fed. 415 (C. C. A. Mass.), quoted at § 1864; In re Friedman, 20 A. B. R. 37, 161 Fed. 260 (C. C. A. N. Y.); In re Peacock, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.); In re Ironclad Mfg. Co., 27 A. B. R. 490, 191 Fed. 831 (C. C. A. N. Y.); *Johnston v. Spencer*, 27 A. B. R. 800, 195 Fed. 215 (C. C. A. Colo.); *First Nat'l Bk. v. Hopkins*, 29 A. B. R. 434, 199 Fed. 873 (C. C. A. Ga.); In re Auerbach, 29 A. B. R. 791, 202 Fed. 192 (C. C. A. N. Y.); *Shea v. Lewis*, 30 A. B. R. 436, 206 Fed. 877 (C. C. A. Minn.); In re Famous Clothing Co., 24 A. B. R. 780, 179 Fed. 1015 (D. C. N. Y.); obiter, In re Pickens & Bro., 26 A. B. R. 6, 184 Fed. 954 (D. C. Ga.); In re Cantelo Mfg. Co., 26

the bankrupt. The bankruptcy court had the power to ascertain whether any basis for such claim actually existed at the time of the filing of the petition. The court would then have been bound to enter upon the inquiry, and in so doing would have undoubtedly acted within its jurisdiction, while its conclusion might have been that an adverse claim, not merely colorable, but real, even though fraudulent and voidable, existed in fact, and so that it must decline to finally adjudicate on the merits. If it erred in its rulings either way, its action would be subject to review."

Bank v. Title & Trust Co., 198 U. S. 280, 14 A. B. R. 102, 107 (reversing 11 A. B. R. 79): "But, nevertheless, the District Court had jurisdiction to determine whether it could or could not proceed further."

In *re Baird*, 8 A. B. R. 649 (D. C. Penn.): "When a petition such as this is presented, asking the District Court to make a summary order directing a respondent to surrender the possession of certain property that is alleged by a trustee to belong to the bankrupt's estate, the court has the undoubted right—indeed, it lies under the duty—to examine the ground set up by the respondent for his refusal to deliver possession, and to determine whether a real, and not merely a pretended controversy exists upon this subject."

In *re Kane*, 12 A. B. R. 444, 131 Fed. 386 (D. C. N. Y.): "The referee is quite right where he says the bankruptcy court has jurisdiction to determine in the first instance whether an asserted adverse claim to property is colorable or actual. If it be clearly a nullity, the referee has jurisdiction, and may by summary process require the surrender of the property so withheld to the trustee in bankruptcy. On the other hand, should evidence of a claimant satisfy the referee that an adverse right to such possession and control is asserted in good faith, and there is reasonable cause for believing that the intention of the claimant is to protect an asserted right of ownership and control, then the petition of the trustee should be dismissed. The remedy of the trustee for the recovery of the property may then be found in a plenary suit instituted in the proper tribunal."

Compare, In *re Friedman*, 18 A. B. R. 712, 153 Fed. 939 (D. C.), affirmed in 20 A. B. R. 37, 161 Fed. 260 (C. C. A.): "But if property which had once been in the possession of the bankrupt is found in the possession of any person, and such person is, in the opinion of the court, very clearly but a cover or receptacle for that property which as between the bankrupt and such other person is still the property of the bankrupt, or if (to vary the simile) the person who holds property which was formerly in the possession of the bankrupt is but the alter ego of the bankrupt, then a summary order is proper, and no pretended instruments of transfer, no apparatus of conveyances, should prevail. The question is: Whose is the property? And if, according to the evidence, it be the property of the bankrupt, the bankruptcy court should order its restoration to the representative of the creditors and enforce that order by the most drastic means. If this be not done, creditors in most cases are utterly without remedy, for a plenary suit against persons who are in truth but receivers of stolen goods (or money) is but an expensive illusion. In this case an unusually complicated scheme was pursued to hide the proceeds of the sale of the bankrupt stock. The complication of the method only renders more necessary the application of the rule which, I believe, exists."

A. B. R. 57, 185 Fed. 276 (D. C. Me.), though this case seems extreme; In *re Franklin, etc., Co.*, 28 A. B. R. 278, 197 Fed. 591 (D. C. Pa.); In *re Logan*, 28 A. B. R. 543, 196 Fed. 678 (D. C. N. Y.); In *re Kreuger*, 28 A. B. R. 890, 196 Fed. 705 (D. C. Ky.).

Obiter, In *re Norris*, 24 A. B. R. 444, 177 Fed. 598 (D. C. N. Y.): "The court has power to ascertain, if an adverse claim be made by a third person in possession of the property whether such claim is in fact well founded, or if it is fictitious or colorable."

In *re Ellis Bros. Printing Co.*, 19 A. B. R. 472, 156 Fed. 430 (D. C. N. Y.): “* * * the bankruptcy court has power to inquire into the facts for the purpose of determining whether any basis exists for the adverse claim of title to the property asserted by the respondent. The mere assertion of an adverse claim of title, even with an intention to protect it by the usual process of law, will not preclude the bankruptcy court from exercising its power to proceed summarily. In *re Andre*, 13 Am. B. R. 132, 135 Fed. 736, 68 C. C. A. 374. It is only when the evidence indicates that the asserted claim is not false or fraudulent that the bankruptcy court is deprived of jurisdiction. If it should appear from the proofs that the respondent, Strong, refuses to surrender the money collected by him to the trustee simply on the ground that the title to the same is conclusively evidenced by his possession of it, or if the claim is unreal or colorable, then it is the duty of this court to direct its payment to the trustee. This principle of law is so clearly and definitely stated by the Supreme Court in *Mueller v. Nugent*, 184 U. S. 1, 7 Am. B. R. 224, * * * that no other citations are thought necessary. In the prior cases decided by this court, in passing upon the right to exercise summary jurisdiction it is not intended to be understood as holding that, irrespective of whether the elicited facts were sufficient in law, the mere assertion of an adverse claim of title or ownership deprived the court of summary power. If the proofs show that in fact there is no legal basis for the asserted adverse claim, the summary power of the court is not defeated.”

And summary jurisdiction has been enforced against the bankrupt's attorney to compel him to surrender money collected by him for the bankrupt before bankruptcy, though he claimed the right to apply it on unpaid attorney's fees;⁸ but this doctrine is valid only within certain limits.^{8a}

The referee has jurisdiction to make the summary order.⁹

In *re Holbrook Shoe & Leather Co.*, 21 A. B. R. 511, 165 Fed. 973 (D. C. Mont.): “A very careful study of the record certified in this matter leads me to conclude that it was the duty of the referee to hear the testimony, in order to pass upon the question whether the claim of the Packard Shoe Company to the property in its possession had an actual basis—that is, was it a real or merely colorable claim? Power and duty to make such inquiry must exist under the Bankruptcy Act, else we cannot escape from the illogical conclusion that the mere assertion of what may be designated an adverse claim can oust the summary jurisdiction of the bankruptcy court, and, as a result, the trustee cannot expeditiously collect the estate for the creditors. But we are not without judicial authority in the premises, as the Supreme Court has expressly declared there is no such ouster, and that jurisdiction exists. *Mueller v. Nugent*, 184 U. S. 1, 7 Am. B. R. 224. But how much farther may the bankruptcy court go? * * * Manifestly, the statute requires a broader construction, one that not alone authorizes the inquiry of the hearing of testimony, but which also required a decision upon the merits by the referee. This decision may be that the claim is in good faith, but of doubtful validity, or of questionable faith, yet is probably real; and, hence, that there ought to be an independent suit brought to try the questions; but if the decision is that the claim is without any actual merit or legal founda-

8. In *re Ellis Bros. Printing Co.*, 19 A. B. R. 472, 156 Fed. 430 (D. C. N. Y.), quoted at §§ 1828, 2099.

8a. Compare post, § 2099.

9. In *re Scherber*, 12 A. B. R. 618, 131 Fed. 121 (D. C. Mass.); In *re Steuer*, 5 A. B. R. 209, 104 Fed. 323 (D. C. Mass.); *Knapp & Spencer v. Drew*, 20 A. B. R. 355, 160 Fed. 413 (C.

C. A. Neb.); In *re Hayden*, 22 A. B. R. 764, 172 Fed. 623 (D. C. Mass.), quoted at § 1864; In *re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.); In *re Tarbox*, 26 A. B. R. 432, 185 Fed. 985 (D. C. Mass.), quoted at § 1864; In *re Logan*, 28 A. B. R. 543, 196 Fed. 678 (D. C. N. Y.).

tion, the referee should regard the property as subject to the jurisdiction of the bankruptcy court, as property of the bankrupt, and should, therefore, proceed to make an order requiring the actual wrongful holder to surrender to the court or trustee."

§ 1864. But Will Only Examine Far Enough to Ascertain if Facts Alleged in Good Faith and if True Would Constitute "Adverse" Party.—But the bankruptcy court will only examine far enough to determine whether the facts are alleged in good faith, that is to say are really considered by the respondent to have actually occurred (even though they constitute fraud in fact), and whether, if true, they would constitute the adverse party an "adverse claimant" within the meaning of the law.¹⁰

In *re Tarbox*, 26 A. B. R. 432, 185 Fed. 985 (D. C. Mass.): "The referee has jurisdiction under a summary petition to inquire and decide whether or not the claim under which property is held adversely to the trustee is merely colorable. But, unless he can find it merely colorable, he has no jurisdiction to proceed further. *Re Hayden* (D. C. Mass.), 22 Am. B. R. 764, 172 Fed. 623. He cannot hear and determine its merits under a summary petition, if there is a real controversy as to the merits. Plainly the trustee cannot enlarge the referee's jurisdiction merely by alleging that the claim under which the property is held has no merits or is fraudulent, or by calling it "merely colorable," when no other reasons appear for so describing it than its alleged want of merit or fraudulent character.

"In this case the referee was informed by the petition that the property had never been in the trustee's possession, that Mrs. Piper claimed it under a mortgage, and that the trustee intended to attack the mortgage on the ground that it was given in fraud of creditors and was, therefore, invalid as against him. I think the referee was right in holding that a mortgagee making such a claim could not be summarily ordered to surrender the property in her possession.

* * *

"To say that the trustee was bound to inquire whether the mortgagee's title was merely colorable, or not, would in this case be to say that he was bound to try the question whether the mortgage was fraudulent, or not, and to disregard the rule above stated."

Impliedly, In *re Auerbach*, 29 A. B. R. 791, 202 Fed. 192 (C. C. A. N. Y.): "It is not necessary to discuss the merits. The special master found discrepancies in Schwartz's testimony, and apparently doubted the accuracy of some of his statements; nevertheless he reached the conclusion that enough was shown to entitle him to have the question of title disposed of in a plenary suit. The District Judge found the case was 'undoubtedly a very suspicious one,' neverthe-

10. In *re N. Y. Wheel Wks.*, 13 A. B. R. 60, 132 Fed. 203 (D. C. N. Y.); In *re Sheinbaum*, 5 A. B. R. 187, 107 Fed. 247 (D. C. N. Y.); In *re Sunseri*, 18 A. B. R. 235 (D. C. Penn.); instance, In *re Eurich's Fort Hamilton Brew*, 19 A. B. R. 798, 158 Fed. 644 (D. C. N. Y.); apparently, In *re Peacock*, 24 A. B. R. 159, 178 Fed. 851 (D. C. N. Car.); *Shea v. Lewis*, 30 A. B. R. 436, 206 Fed. 877 (C. C. A. Minn.); In *re Rathman*, 25 A. B. R. 246, 183 Fed. 913 (C. C. A. S. D.); In *re Famous Clothing Co.*, 24 A. B. R. 780, 179 Fed. 1015 (D. C. N. Y.); In *re Bacon*, 28 A. B. R. 565, 196 Fed. 986 (D. C.

N. Y.); In *re Carlile*, 29 A. B. R. 373, 199 Fed. 612 (D. C. N. Car.); *Johnston v. Spencer*, 27 A. B. R. 800, 195 Fed. 215 (C. C. A. Colo.); in effect, In *re Pickens & Bro.*, 26 A. B. R. 6, 184 Fed. 954 (D. C. Ga.).

But compare, extreme case, where the estoppel of an inventor from claiming pending applications for patents, as against the trustee of the bankrupt corporation by which he had been employed to invent, made him only a "colorable" adverse claimant. In *re Cantelo Mfg. Co.*, 26 A. B. R. 57, 185 Fed. 276 (D. C. Me.).

less he thought it preferable to have it so tried. Such a plenary suit being then pending in the State court; the case was appropriately left to it to decide."

In *re Kane*, 12 A. B. R. 444, 131 Fed. 386 (D. C. N. Y.): "If he is satisfied, either from personal knowledge of the facts or from testimony, that an order to show cause ought to be directed to a person charged with having in his possession property belonging to the bankrupt estate, the essential inquiry upon return of the order to show cause, if an adverse claim is made, is whether such claim is colorable or fictitious. In short, if it is a colorable claim, it should be set aside, and the claimant summarily directed to deliver the property to the trustee; but if, as already indicated, the claim is asserted in good faith, substantiated by verified pleadings or by oral testimony, then the objection to the jurisdiction of the court is controlling. In such an event the property is no longer constructively in the possession of the bankrupt and subject to the order of the bankruptcy court."

In *re Teschmacher & Mrazay*, 11 A. B. R. 547, 127 Fed. 728 (D. C. Pa.): "As I understand the decisions of the Supreme Court * * * a court of bankruptcy, before the amendments of 1903 were passed, had jurisdiction to inquire summarily upon petition and answer whether property alleged to belong to the bankrupt, but found in the possession of a third person when the petition was filed, was held by such person as the bankrupt's agent or mere representative; and in the exercise of this jurisdiction the court was of necessity empowered to inquire to some extent concerning the merits of the claim of title, or of a right to retain possession, that might be set up by the person in whose hands the property was found. If the result of the inquiry was to satisfy the court that a real adverse claim existed—no matter how ill-supported it might appear to be—the court had no power to go further in that form of proceeding and decide summarily the question whether or not the claimant was entitled to prevail. It then became necessary, because the Bankrupt Act so declared, to remit the contestants to a plenary suit, either in a State court or in a Circuit Court of the United States, whichever might prove to be the appropriate tribunal. In either forum, however, the dispute was to be conducted by a plenary suit, and not in a summary fashion. The amendments of 1903, as I understand their scope, have made at least one change in these rules. They have conferred jurisdiction upon the District Court to entertain some of the plenary suits which theretofore could only have been brought in a State court or in the Circuit Court, but the other rules of procedure laid down by the Supreme Court are still to be followed. The District Court, sitting as a court of bankruptcy, may still inquire summarily concerning the ownership of property alleged to belong to the bankrupt, although it be found in the possession or custody of a third person. But, if the court should discover that such person is holding the property under a real claim of title or right of possession, and is not merely the alter ego of the bankrupt, it is still the duty of the court to desist from pursuing the summary remedy further, and to remit the contestants to a plenary suit, although the suit, instead of being brought in a State court or a Circuit Court of the United States, may now be brought in the District Court itself, and may there be pursued to final judgment."

In *re Baird*, 8 A. B. R. 649 (D. C. Penn.): "And when it appears, as I think it sufficiently appears in the present case, that in some of its aspects, at least, the controversy requires a court to decide upon the validity of a real claim to the property in question, in my opinion the District Court is obliged to decline the jurisdiction, and to refer the matter to the appropriate tribunal of the State. To decide that the claim is unfounded would be to assume the jurisdiction that is denied by the act. The order I am about to make, however, must not be regarded as impairing in any respect the effect of the order heretofore entered upon the petition of the Juniata Limestone Company."

In re Adams, 12 A. B. R. 367, 130 Fed. 788 (D. C. R. I.): "The claim of Nass that, before the filing of the petition in bankruptcy, he had received the property in question as part payment of a debt, and that he had no reasonable cause to believe that it was intended thereby to give a preference, was clearly an adverse claim. * * * The referee, however, found as facts that the taking of possession by Nass was without authority from Adams; that Nass knew, or had reasonable cause to know, that the taking constituted a preference, and that the taking of the property was equivalent to trover and conversion, and carried no title; that, in consequence thereof, Nass had not even a colorable claim to title. This was not a decision that, upon the facts as claimed by Nass, he was not an adverse claimant, nor an inquiry into the existence of an adverse claim; but a decision of the merits of an adverse claim of right, and a finding that the claim was not adverse because, in the opinion of the referee it was not, as a matter of evidence, meritorious in point of fact. As it is clear from the report of the referee, and from his decree, that Nass was, properly speaking, an adverse claimant, the referee, upon objection should have declined to finally adjudicate the merits of the case on summary petition."

Instance, In re Eddleman, 19 A. B. R. 45, 154 Fed. 160 (D. C. Ky.): "The evidence, however, further shows that \$1,605 of the money was paid out by the wife to Mrs. Fredericka Nickel, to whom she owed a note for borrowed money. This payment seems to have been made before the petition in bankruptcy was filed. There may not be any presumption that it was so, yet it is possible that this transaction may have been a fraudulent one—a mere friendly contrivance. Nevertheless, it is fair to assume that Mrs. Nickel thereby acquired what is called by the Supreme Court, in *Mueller v. Nugent*, 184 U. S. at page 15, 7 Am. B. R. 224, a basis for an adverse claim to that much of the \$2,057.29, and, if so, we can hardly see how we can punish the bankrupt for contempt for not paying over the money which the testimony shows was, presumably at least, adversely claimed by another person."

In re Hayden, 22 A. B. R. 764, 172 Fed. 623 (D. C. Mass.): "It was the referee's duty to inquire whether any basis for such a claim to the property as that asserted by the three respondents above named actually existed at the time of the filing of the petition. He was bound to enter upon that inquiry, and in doing so undoubtedly acted within his jurisdiction. It was for him to ascertain whether the respondents' claim to hold the property against the trustee was really adverse, as would appear from their answers, or was merely colorable. * * * For this purpose and to this extent he had jurisdiction to investigate the merits of the questions raised. If, however, as the result of his investigation he found the claim to be really adverse, it followed from that conclusion that he was without jurisdiction to proceed further."

In re Tune, 8 A. B. R. 285, 115 Fed. 906 (D. C. Ala.): "Summary jurisdiction is ousted if determination of the validity of the adverse claim involves the decision of matters in pais and the weighing of conflicting evidence and finding of facts, which, when presented leave room for fair doubt as to the invalidity of the claim, since such a claim is not merely colorable. Delivery must then be compelled by suit in plenary proceedings in a proper court."

In re Horgan, 21 A. B. R. 31, 164 Fed. 415 (C. C. A. Mass.): "But one question is here presented: Was the petitioners' claim to the sum here in controversy, * * * a claim really adverse to * * * the trustees in bankruptcy or merely colorably so? The District Court had jurisdiction to pass upon this question; but, if the claim was really adverse, the court was without jurisdiction to proceed further under § 23 of the Bankruptcy Act. * * * Whether the lien claimed by the petitioners be deemed to arise by implication of law out of the deposit with them of security for their liability on the bail bond, or from the express contract set up in their affidavits, we are of

opinion that their claim to the lien was not so clearly without foundation as to be merely colorable within the decisions of the Supreme Court. * * * We are not called upon to hold the petitioners' claim to be valid, and we do not so hold. We merely hold it to be really adverse to the claim of the trustees in bankruptcy."

And the court is bound to enter on the inquiry to ascertain whether an adverse claim, not merely colorable, but real, even though fraudulent and voidable, exists in fact.¹¹

§ 1865. Whether Concluded by Pleadings.—The bankruptcy court, it appears, is not concluded by the pleadings, but may inquire into the facts to see if the claim is really adverse or merely colorably so; if really adverse, although fraudulent and voidable, or not sustainable by the weight of the evidence, jurisdiction will not be assumed.¹²

Mueller v. Nugent, 184 U. S. 1, 7 A. B. R. 224, 235: "But suppose that respondent had asserted that he had the right to possession by reason of a claim adverse to the bankrupt, the bankruptcy court had the power to ascertain whether any basis for such a claim actually existed at the time of the filing of the petition. The court would have been bound to enter upon that inquiry, and in doing so would have undoubtedly acted within its jurisdiction, while its conclusion might have been that an adverse claim, not merely colorable, but real even though fraudulent and voidable, existed in fact, and so that it must decline to finally adjudicate on the merits. If it erred in its ruling either way, its action would be subject to review."

In re Kane, 12 A. B. R. 444, 131 Fed. 386 (D. C. N. Y.): "The referee is quite right when he says the bankruptcy court has jurisdiction to determine in the first instance whether an asserted adverse claim to property is colorable or actual. * * * The determination of the respective rights of the parties demands judicial investigation by the referee to ascertain the facts. Both sides are heard, and evidence may be taken though the conclusions of the court may be based upon the pleadings or affidavits presented to him. He must exercise a sound judicial discretion in the determination of questions of this character to the end that no injustice be done to either party."

Compare, *In re Baird*, 8 A. B. R. 650 (D. C. Pa.): "To decide that the claim is unfounded would be to assume the jurisdiction that is denied by the Act."

But the petition for the summary recovery must not fail to state that the adverseness of the claim is merely colorable, else the claim will be taken as really adverse.

In re Scherber, 12 A. B. R. 616, 131 Fed. 121 (D. C. Mass.): "But the respondent's claim in the case at bar is not alleged in the petition to be merely colorable, and must be taken to be really adverse. Where this is true, and where due objection to the form of proceeding is made, the decisions and language of the Supreme Court imply that a plenary suit must be resorted to."

And where the trustee's petition itself shows claimants' adverseness, evi-

11. *In re Friedman*, 20 A. B. R. 37, 161 Fed. 260 (C. C. A. N. Y.).

12. See ante, § 1863. *In re Michie*, 8 A. B. R. 734, 115 Fed. 906 (D. C. Mass.). Compare, *In re Adams*, 12 A. B. R. 367, 130 Fed. 788 (D. C. R. I.); *In re N. Y. Wheel Wks.*, 13 A. B. R. 60, 132 Fed. 203 (D. C. N. Y.); *In re Sheinbaum*, 5 A. B. R. 187, 107 Fed.

247 (D. C. N. Y.); *In re Ironclad Mfg. Co.*, 27 A. B. R. 490, 191 Fed. 831 (C. C. A. N. Y.); *Johnston v. Spencer*, 27 A. B. R. 800, 195 Fed. 215 (C. C. A. Colo.); *In re Mimms & Parham*, 27 A. B. R. 469, 193 Fed. 276 (D. C. Ky.); impliedly, *In re Pickens & Bros.*, 26 A. B. R. 6, 184 Fed. 954 (D. C. Ga.).

dence that such claim was merely colorable should be excluded.^{12a}

But, it would seem to be the better rule that, unless the bad faith were sufficient to warrant a court in striking the pleadings from the files, the pleadings, especially if positively verified, should bind the court as to whether summary jurisdiction exists; so that, in general, existence of summary jurisdiction would be rather a question of allegation than of proof.

Cooney v. Collins, 23 A. B. R. 840, 176 Fed. 189 (C. C. A. Montana): "All of the above-mentioned allegations of the defendant John W. Cooney were verified by him of his own knowledge. His objections to the determination, in such summary proceedings, of the right to the properties in question, were overruled by the referee in bankruptcy, which officer found, in effect, upon the conflicting evidence introduced before him, that all of the property in question really belonged to the bankrupt, Frank Henry Cooney, was paid for with his money, and put in the name of John W. Cooney for the purpose of defrauding the creditors of Frank Henry Cooney. The matter being brought before the court upon petition for revision of the action of the referee, like objections were there made by John W. Cooney to the jurisdiction of the referee, and of the power of the bankruptcy court to thus determine the property rights in question, resulting in the affirmance by the court of the referee's order. Hence the present petition for review. In so ruling we are of the opinion that the learned judge of the court below was in error. That court, as well as the counsel for the respondent here, largely rely in support of their position upon the case of *Mueller v. Nugent*, 184 U. S. 1, 7 Am. B. R. 224, which case was subsequently reviewed in the case of *Jaquith v. Rowley*, 188 U. S. 620, 624, 9 A. B. R. 525, where the Supreme Court thus concluded its review of it: 'in other words, *Nugent's* case simply holds that where the agent held money belonging to the bankrupt to which he had no claim, but simply refused to give up the property, which he acknowledged belonged to the bankrupt, the bankruptcy court had power, by summary proceedings, to order him to deliver such property to the trustee in bankruptcy, which was not only a "wholly different" case from that of *Jaquith v. Rowley*, but also from that now before us. Like the surety in the case of *Jaquith v. Rowley*, the petitioner here, John W. Cooney, by his verified answer not only claims the absolute right to hold all of the property in question as against everybody, but specifically alleges the reasons for his claim of ownership of it. Of course, his allegations in that behalf may not be true; still they make a case of adverse claim to the property on his part, to overcome which it was essential for the trustee to protect in accordance with the provisions of § 23 of the Bankruptcy Act and not by summary proceeding in bankruptcy. We think the case of *Jaquith v. Rowley*, 188 U. S. 620, 9 Am. B. R. 525, is directly in point, on the authority of which the judgment of the District Court should be reversed, with directions to order the dismissal of the trustee's petition.'"

What is sufficient to make the claim "colorable" is largely a question of the facts of each particular case; yet, if it is to be decided by the pleadings, as is the author's view, then the colorability is easily determinable; for, whether alleged by the trustee or by the adverse claimant, the allegations of actual possession and of facts which, if true, would constitute adverse

^{12a}. In *re Michie*, 8 A. B. R. 734, 115 Fed. 906 (D. C. Mass.); instance, In *re Tarbox*, 26 A. B. R. 432, 185 Fed. 985 (D. C. Mass.), quoted at §§ 1699, 1864.

For form of such petition and notice, see In *re Scherber*, 12 A. B. R. 616 (D. C. Mass.).

title (i. e., that the possession is not under the bankrupt, nor as his agent, nor under the marshal, or receiver, nor trustee in bankruptcy, nor merely as a custodian or stakeholder, but as a party claiming rights in opposition thereto) then the bankruptcy court must refuse to take jurisdiction,¹³ unless the bad faith of the claim is so gross as to warrant the striking of his pleadings from the files under the usual rules in such cases, or unless the allegations of the pleadings are simply mere assertions of ownership or other conclusions of law, in which event it is the duty of the court to cause a preliminary investigation to be made summarily to determine whether or not the claim is merely colorable.¹⁴

In *re Blum*, 29 A. B. R. 330, 202 Fed. 883 (C. C. A. Wis.): "The term 'colorable' seems to have crept into the bankruptcy decisions without authority of statute—unless it be construed to mean merely that if a respondent sets up as facts, and not as conclusions of law, matters which, if true, would constitute a statement of an adverse claim, then the claim would be adverse and not colorable, and not within the jurisdiction of the referee. It can hardly have been the purpose of Congress to deprive a litigant of the benefit of a plenary hearing in cases involving the determination of contested questions of fact. Undoubtedly, one holding property of the bankrupt as an agent or bailee may be required summarily to turn it over to the trustee, and, in a proper case, to a receiver; but we are of the opinion that whenever the facts alleged on their face disclose possession and a legal right in the party claiming title, the referee has no jurisdiction in a summary proceeding to require the property to be turned over without the consent of the respondent. * * * We believe the true rule to be as above stated, viz. that where a party in possession sets out in his answer facts which, if true, would constitute an adverse title, the court may not in a summary proceeding, and against his protest, dispose of his rights in property. It therefore follows in the present case that petitioner was entitled to have her claim adjudicated in a plenary suit."

§ 1866. Notice Served Outside District Not Sufficient to Confer Jurisdiction to Make Inquiry.—Notice served outside the district where the bankruptcy proceedings are pending, upon an "adverse claimant" in possession of the property, will not confer jurisdiction on the bankruptcy court to make the inquiry.¹⁵

In *re Waukesha Water Co.*, 8 A. B. R. 715, 116 Fed. 1009 (D. C. Wis.): "Jurisdiction of the subject matter is undoubted under the recent decision in *Mueller v. Nugent*, 184 U. S. 1, 22 Sup. Ct. 269, 46 L. Ed. 405, 7 A. B. R. 224, and, if adverse claim to the property were asserted by the respondents, the court must ascertain whether it is of that character, and so takes cognizance to that extent at least. It determines for itself whether final jurisdiction exists.

"The questions raised, however, of jurisdiction to act in personam upon these respondents, who reside in another State and District, and are there served with the order to show cause in this matter, is not met by that decision, nor in such service authorized by any express provision of the Bankruptcy Act or

13. Compare ante, §§ 1864, 1865; also compare, In *re Tarbox*, 26 A. B. R. 432, 185 Fed. 985 (D. C. Mass.), quoted at § 1864; In *re Blum*, 29 A. B. R. 332, 202 Fed. 883 (C. C. A. Wisc.), quoted supra; In *re Green*, 30 A. B. R. 464, 207 Fed. 693 (D. C. Pa.).

14. In *re Ironclad Mfg. Co.*, 27 A. B. R. 490, 191 Fed. 831 (C. C. A. N. Y.).

15. In *re Alphin & Lake Cotton Co.*, 12 A. B. R. 654, 131 Fed. 824 (D. C. Ark.). Contra, inferentially, In *re Peiser*, 7 A. B. R. 690, 115 Fed. 199 (D. C. Penn.).

ruling thereunder called to my attention. In the absence of statutory authority for the process of the court to run beyond the territorial limits of the district, the doctrine is well settled that no jurisdiction exists to that end."

§ 1867. Ancillary Jurisdiction in Bankruptcy Court of Another District to Make Summary Order.—As we have previously seen jurisdiction exists in the bankruptcy court of another district in ancillary proceedings there pending to make a summary order to surrender assets in aid of the original bankruptcy proceedings.¹⁶

DIVISION 3.

REDEMPTION OF PROPERTY FROM LIENS.

§ 1868. Jurisdiction to Redeem Property from Liens.—The bankruptcy court has jurisdiction to redeem property from liens and charges.¹⁷

§ 1869. Procedure—Petition to Redeem and Notice.—Redemption may be ordered upon petition and notice. Ten days' notice, it appears from the Supreme Court's Official Form No. 43, is to be sent to all creditors,¹⁸ although § 58 does not specifically mention such applications among those matters notice of which must be sent to all creditors. Likewise, notice should be given to the lienholder, in similar manner to that given in cases of sales free from liens. The petition may be filed before the referee.

§ 1870. Gives Jurisdiction to Order Cancellation, Assignment or Release, on Tender of Amount Due.—In proceedings to redeem, the bankruptcy court has jurisdiction to order cancellation, release or assignment of the lien on tender of the amount due,¹⁹ at any rate if there be no controversy over such amount and no colorable adverse interest.

§ 1871. May Not, under Guise of Petition to Redeem, Gain Jurisdiction Over Adverse Claimants in Possession.—But the filing of the petition to redeem, and service of notice upon the lienholder, will not give jurisdiction over adverse claimants in possession, nor may controversies with them be litigated in such proceedings. The petition to redeem is more in the nature of an application to the court of bankruptcy for leave to pay off an uncontroverted lien than it is a proceedings in the nature of the old equity action for redemption. In case the lien be paid and there is no colorable adverse interest in the lienholder, the bankruptcy court will have jurisdiction under the petition to redeem to summarily order surrender of the property, under its ordinary jurisdiction.

16. Compare ante, "Ancillary Proceedings," § 1705, et seq. Contra, before decision in *Babbitt v. Dutcher* and before the Amendment of 1910. In re Van Hartz, 15 A. B. R. 747, 142 Fed. 726 (C. C. A. N. Y.).

In re Heintz, 29 A. B. R. 19, 201 Fed. 338 (C. C. A. Ohio), quoted at § 1707;

In re Rothfon, 29 A. B. R. 22, 200 Fed. 108 (D. C. Mich.), quoted at § 1707.

17. In re Bacon, 12 A. B. R. 730, 132 Fed. 157 (D. C. N. Y.). Supreme Court's Official Form No. 43.

18. In re Grainger, 20 A. B. R. 166, 173, 160 Fed. 69 (C. C. A. Calif.).

19. In re Bacon, 12 A. B. R. 730, 132 Fed. 157 (D. C. N. Y.).

DIVISION 4.

SUMMARY JURISDICTION TO ORDER TRUSTEE, ETC., TO SURRENDER PROPERTY TO RIGHTFUL OWNERS.

§ 1872. Summary Jurisdiction to Order Trustee to Surrender Property to Rightful Owner.—The bankruptcy court has jurisdiction to determine the rights of third parties claiming property in its custody, and is bound to turn it over to the one entitled thereto,²⁰ and the bankruptcy court has summary jurisdiction over the trustee, to this end.²¹ The proper procedure is for an order to show cause to be issued upon the trustee, upon the claimant's petition, as in other cases.²²

§ 1873. Thus, to Order Surrender of Property Belonging to Third Parties.—And thus the bankruptcy court has jurisdiction to order the surrender or redelivery of property in its custody belonging to third parties.²³ And, as incident thereto, the bankruptcy court may compel the trustee to execute assignments of the property, or other instruments necessary or proper.²⁴

§ 1874. Referee Has Jurisdiction.—A referee has jurisdiction to determine the ownership of property in the possession of a receiver or trustee appointed by the bankruptcy court, where a third party files a petition, or an intervening petition, claiming the ownership of such property.²⁵

^{20.} See cases cited ante, as to jurisdiction of bankruptcy court over property in its custody, § 1795.

Summary Jurisdiction over Trustee as to Exceptions to His Accounts.—The bankruptcy court in general has summary jurisdiction over the trustee or receiver in respect to their accounts. Impliedly, *In re Moore & Bridgeman*, 21 A. B. R. 651, 166 Fed. 689 (C. C. A. Tex.).

^{21.} Instance, *In re MacDougall*, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.).

^{22.} Instance, *In re MacDougall*, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.).

^{23.} *Havens v. Pierek*, 9 A. B. R. 569, 120 Fed. 244 (C. C. A. Ills.); *In re J. C. Winship Co.*, 9 A. B. R. 641, 120 Fed. 93 (C. C. A. Ills.); *In re White-ner*, 5 A. B. R. 198, 105 Fed. 180 (C. C. A. Tenn.); *In re Sentenne & Green Co.*, 9 A. B. R. 648, 120 Fed. 436 (D. C. N. Y.); *In re McCallum*, 7 A. B. R. 596, 113 Fed. 393 (D. C. Pa.); *In re Hadden-Rodee Co.*, 13 A. B. R. 604, 606, 135 Fed. 886 (D. C. Wis.); *obiter*, *In re Rochford*, 10 A. B. R. 608, 124 Fed. 184 (C. C. A. S. Dak.); *In re Moody*, 12 A. B. R. 725, 131 Fed. 525

(D. C. Iowa); *In re Condon*, 28 A. B. R. 851, 198 Fed. 480 (C. C. A. N. Y.); instance, *In re Thompson*, 30 A. B. R. 64, 208 Fed. 207 (D. C. N. Y.).

^{24.} *In re McBride & Co.*, 12 A. B. R. 81, 132 Fed. 285 (Ref. N. Y.), in which case the court ordered the trustee to execute an assignment of a copyright standing in the bankrupt's name but belonging to another.

[Release] *Kenyon v. Mulert*, 26 A. B. R. 184, 184 Fed. 825 (C. C. A. Pa.).

^{25.} *In re Drayton*, 13 A. B. R. 602, 135 Fed. 883 (D. C. Wis.); *In re Scrinopski*, 10 A. B. R. 221 (D. C. Kans.); compare, *Carriage Co. v. Sol-lanas*, 6 A. B. R. 221, 108 Fed. 532 (D. C. La.); *In re Neely*, 5 A. B. R. 836, 108 Fed. 371 (D. C. N. Y.); *In re Coffey*, 19 A. B. R. 148 (Ref. N. Y.).

Apparently, contra, and that a "plenary action" is proper, *In re Rus-sell & Birkett*, 3 A. B. R. 658 (C. C. A. N. Y.); impliedly, *In re McBride & Co.*, 12 A. B. R. 81, 132 Fed. 285 (Ref. N. Y.).

Impliedly, *In re Rochford*, 10 A. B. R. 608, 124 Fed. 184 (C. C. A. S. Dak.), which was, however, a case of a lien upon, rather than a claim to, property in the hands of the trustee; yet the principle is the same.

§ 1875. **Replevin Suits Not Maintainable against Trustee or Receiver.**—Adverse claimants to any of the property must not resort to legal proceedings in other courts, or other methods of seizure or of taking possession of property in the custody of the bankruptcy court. They must come into the bankruptcy court and make application there for a return of the property,²⁶ excepting, possibly, as to property to which the trustee has failed to assert ownership.²⁷

§ 1876. **Petitions for Reclamation, Surrender or Redelivery.**—Surrender of property in the custody of the bankruptcy court but belonging to a stranger, is accomplished by filing before the referee a petition, variously styled a petition for redelivery, for surrender, for restitution or for reclamation.²⁸ A “proof of debt” is not a proper method.²⁹

These petitions should set up the facts, in accordance with the ordinary rules of pleading in an action of trover, conversion or replevin, that would entitle the claimant to the property.

Levi v. Picard, 17 A. B. R. 431, 148 Fed. 654 (D. C. N. Y.): “Viewing the petition in reclamation as a pleading, it seems to me obvious that it should contain all the allegations necessary to sustain a complaint in trover and conversion, or required by the strictest practice in an affidavit for replevin.”

But it has been held that in reclamation proceedings, it is not necessary that the petition should describe the property claimed with that degree of definiteness and particularity required in a complaint and writ in an action of replevin.

In *re Pierce*, 19 A. B. R. 664, 157 Fed. 757 (C. C. A. N. Dak.): “It is contended that the petition to the bankruptcy court is fatally defective because

26. See cases cited under §§ 1794, 1795, et seq. Also see *Murphy v. John Hoffman Co.*, 21 A. B. R. 487, 211 U. S. 562; *White v. Schloerb*, 4 A. B. R. 178, 178 U. S. 542; *Berman v. Smith*, 22 A. B. R. 662, 171 Fed. 735 (D. C. Ga.). Contra, In *re Smith*, 9 A. B. R. 590 (D. C. R. I.), where the court seems to have assumed the right of the claimant to replevy and refused to enjoin.

And see also, apparently, contra, In *re Freeman*, 9 A. B. R. 68 (D. C. N. Y.), wherein the court seems to have assumed the right of the claimant to replevy from the trustee, and is concerned solely with the merits of a compromise of the controversy involved.

27. Instance, *Kellogg, etc., Co. v. Curtice*, 28 A. B. R. 906 (Ct. App. Mo.).

28. The trustee may himself file a petition for authority to surrender the property, without any action on the claimant's part. Instance, *McDonald v. Clearwater Ry. Co.*, 21 A. B. R. 182,

164 Fed. 1007 (U. S. C. C. Idaho). And in one instance the court dispensed with formal reclamation proceedings and ordered the return of goods without a petition being filed, In *re Kingston Realty Co.*, 19 A. B. R. 703, 157 Fed. 303 (D. C. N. Y.), which is, however, a practice not to be commended.

Payments to Trustees under Mistake of Law.—If money is paid or property turned over to a trustee in bankruptcy under mistake of law it should be surrendered to the rightful owner, the rule being different with court officers from what it is with individuals, obiter, *Carpenter v. Southworth*, 21 A. B. R. 390, 165 Fed. 428 (C. C. A. N. Y.); but it should not be surrendered even though at law not recoverable, if justly it should be retained. *Carpenter v. Southworth*, 21 A. B. R. 390, 165 Fed. 428 (C. C. A. N. Y.).

29. In *re Dorr*, 21 A. B. R. 752 (Ref. Calif.).

the property claimed was not specifically described. It is not necessary in cases of this sort that the property claimed be described with that degree of definiteness and particularity that is required in a complaint and writ in an action in replevin. It not infrequently happens that the claimant is unable to give in the first instance more than a general description of his property, and is compelled to rely upon the proofs at the hearing for its separation from other property of similar kind. A court of bankruptcy exercising equity powers may be depended upon to see that justice is done, and that no more is secured by the claimant than he is entitled to. Moreover, in the present case there were attached to the petition of the company invoices in which the property delivered under the contract was described minutely and in detail, and reference was made to them in the body of the petition. The order of the referee directing surrender to the claimant contained a like reference. This was sufficient in a case of this character."

Notice should be served on the trustee; answer should be filed by him, and due hearing be had.³⁰ Thus, the hearing was held to have been too summary, where, in answer to the claimant's sworn petition, the receiver appears merely to have submitted a receipt and the judge thereupon to have concluded the hearing and forthwith ordered dismissal of the petition.³¹

The hearing should not be had upon affidavits,³² for the proceedings correspond to an action of replevin; for which reason it is that the pleading is styled a petition, rather than a motion.³³

A deposition for proof of debt, though given probative effect, as prima facie evidence of a "claim," is not to be held evidence in a petition for reclamation, as apparently was the obiter holding in one case.³⁴ Indeed, such deposition, being that provided for proof of debts, would, rather, be an implied ratification of the conversion and an admission that a mere debt exists—a waiver of the tort and a claiming upon the contract.³⁵

After the case has been closed it should not be reopened for the ad-

30. Compare practice on objections to claims, ante, § 841.

31. In re Corn, 24 A. B. R. 681, 178 Fed. 841 (C. C. A. N. Y.).

Reclaimant giving bond voluntarily on removal of fixtures reclaimed by him. In re Regealed Ice Co., 29 A. B. R. 69, 199 Fed. 340 (D. C. R. I.).

32. Analogously, In re Bailey, 19 A. B. R. 470, 156 Fed. 691 (D. C. N. Y.).

33. However, in one case the court relegated the parties to a plenary action under the impression that the hearing otherwise would be upon affidavits, which the court evidently deemed inadequate. In re Mundle, 13 A. B. R. 490 and 14 A. B. R. 680, 139 Fed. 691 (D. C. N. Y.). Compare, In re Russell & Birkett, 3 A. B. R. 658 (C. C. A. N. Y.).

Not Triable to Jury.—Such petitions for reclamation are not triable to a jury. They are strictly in equity. *Dokken v. Page*, 17 A. B. R. 228, 147 Fed. 438 (C. C. A. N. Dak.).

Demurrer seems to have been permitted in an analogous case where the validity of a lien was in question and all the allegations considered together and legal conclusions disregarded. In re Gosch, 9 A. B. R. 613, 121 Fed. 604 (D. C. Ga.).

Costs on Dismissal of Reclamation Petition.—Expense of preserving the property pending the hearing upon an unsuccessful petition for reclamation may be taxed against the claimant. In re Schocket (Ex parte Blankenstein), 24 A. B. R. 47, 177 Fed. 583 (D. C. R. I.).

When receiver's and trustee's commissions chargeable on granting petition for reclamation, see post, § 2111.

34. See ante, § 844; obiter, In re McIntyre & Co., 24 A. B. R. 1, 176 Fed. 552 (C. C. A. N. Y.).

35. See ante, § 844; impliedly holding evidence of conversion, In re McIntyre & Co., 24 A. B. R. 1, 176 Fed. 552 (C. C. A. N. Y.).

mission of further testimony except upon good cause shown, in accordance with the ordinary rules.³⁶

Of course, at the time of bankruptcy there are likely to be many articles in the bankrupt's possession that really do not belong to him and therefore do not belong to his creditors.³⁷

§ 1877. Reclamation of Property Left for Repairs, Storage or Other Bailment.—Thus, goods left with him for repairs, or on storage, or on other bailment, may be reclaimed;³⁸ likewise goods shipped to the bankrupt to be treated by him and then reshipped to the customer.³⁹

§ 1877¼. Of Property Sold on Approval, etc.—Thus, property sold to the bankrupt on approval and not accepted or where title has not passed for other reasons, may be reclaimed,⁴⁰ as goods sold on "sale and return"⁴¹ and goods sold with bill of lading attached to draft;⁴² also articles leased, with option to purchase not exercised within the time limited, but payment of rent continued.⁴³

§ 1877½. Of Consigned Property.—Property left on consignment may be reclaimed.

Mathieu v. Goldberg, 19 A. B. R. 191, 156 Fed. 541 (D. C. N. Y.): "But the general rule I understand to be that a principal in the absence of an

36. In re Booss, 18 A. B. R. 658, 154 Fed. 494 (D. C. Pa.), quoted at § 553½.

37. **Infant Repudiating an Otherwise Preferential Bill of Sale, No Right to Priority on Theory of Return of Money Loaned by Him.**—Where, after an infant's claim as a preferred creditor under a bill of sale given within the four months period, has been disallowed, because possession of the property covered thereby had not been given prior to the bankruptcy, the claimant, upon electing to disaffirm the bill of sale will be treated as a general creditor upon seeking to prove a claim for the loans made by him to the bankrupt. In re Huntenberg, 18 A. B. R. 697, 153 Fed. 768 (D. C. N. Y.).

Res Judicata and Collateral Attack.—As to questions of res judicata and collateral attack arising in such proceedings, compare, § 1771, et seq.; also, compare, *Ross v. Stroh*, 21 A. B. R. 644, 165 Fed. 628 (C. C. A. Pa.).

No estoppel, after creditors refuse offer of composition because of adverse claimant's standing by silently without claiming ownership before refusal, In re Loll, 20 A. B. R. 548, 162 Fed. 79 (D. C. Conn.).

38. Instance, reclamation granted, bailment with option to purchase

after trial, In re Rubber Ref. Co., 15 A. B. R. 72, 139 Fed. 201 (D. C. Penn.).

Instance, reclamation refused, bill of sale found fraudulent, In re Schlessel, 18 A. B. R. 429 (Ref. N. Y.); instance, reclamation granted where verbal assignment of book accounts made and trustee collected same, In re Macaulley, 18 A. B. R. 459, 158 Fed. 322 (D. C. Mich.); reclamation where patented articles left to be sold under terms of license, In re Spitzel & Co., 21 A. B. R. 729, 168 Fed. 156 (D. C. N. Y.).

In re Reynolds, 29 A. B. R. 145, 203 Fed. 162 (D. C. Ky.); In re Smith, 27 A. B. R. 647, 192 Fed. 574 (D. C. Md.); In re Marx Tailoring Co., 28 A. B. R. 147, 196 Fed. 243 (D. C. Ala.); Liquid Carbonic Co. v. Quick, 25 A. B. R. 594, 182 Fed. 603 (C. C. A. Pa.).

39. In re Susquehanna Roofing Co., 23 A. B. R. 5, 173 Fed. 150 (D. C. Ark.).

40. In re Planett Mfg. Co. (Schultz v. Scott), 19 A. B. R. 729, 157 Fed. 916 (C. C. A. Ind.); Pridmore v. Puffer Mfg. Co., 20 A. B. R. 851, 163 Fed. 496 (C. C. A. S. Car.).

41. In re Schindler, 19 A. B. R. 800, 158 Fed. 458 (D. C. N. Y.).

42. In re Reboulin Fils & Co., 21 A. B. R. 296, 165 Fed. 245 (D. C. N. J.).

43. *McEwen v. Totten*, 21 A. B. R. 336, 164 Fed. 837 (C. C. A. Ga.).

agreement, express or implied, to the contrary, has a right at any time to retake possession of unsold goods consigned to a factor, on payment of all advances and liens (19 Cyc., p. 117, and cases cited); and I do not think that the fact that Goldberg, under the arrangement, was to be paid for his services by a part of the profits instead of by the usual percentage makes the rule inapplicable."

Likewise, where, by contract, the proceeds of property left on consignment were to be held as a trust fund for the benefit of the seller, such proceeds, if kept separate at any rate, are reclaimable.⁴⁴

Similarly, a bank has been granted reclamation of goods and of the proceeds of goods held in trust by the bankrupt under an arrangement whereby it had accepted and paid drafts for their purchase price, as they were imported from time to time, receiving bills of lading which it had immediately exchanged for trust receipts of the purchaser who had agreed therein to hold and sell the goods for the account of the bank as security for the advances, the bank having reserved the right at any time to cancel the trust arrangement and take possession of the goods.⁴⁵

§ 1878. Of Property Bought on Conditional Sale.—Property sold to the bankrupt on conditional sale is reclaimable—where it would be reclaimable under state law.⁴⁶

York Mfg. Co. v. Brewster, 23 A. B. R. 474, 174 Fed. 566 (C. C. A. Tex.): "The appellant is entitled to have its property restored (In re Great Western Mfg. Co.); or, in lieu of the property, to payment of the debt to it according

44. In re McGehee, 21 A. B. R. 656, 166 Fed. 928 (D. C. Ga.), quoted at § 1883.

45. In re Cattus, 26 A. B. R. 348, 183 Fed. 733 (C. C. A. N. Y.), quoted at § 1150; In re Coe, 26 A. B. R. 352, 183 Fed. 745 (C. C. A. N. Y.).

46. Instance, loans sold on conditional sale. *Davis v. Crompton*, 20 A. B. R. 53, 158 Fed. 735 (C. C. A. Pa.); instance, implements, In re Pierce, 19 A. B. R. 664, 157 Fed. 757 (C. C. A. N. D.); instance, steel rails, *Nat'l Bank v. Williams*, 20 A. B. R. 79, 159 Fed. 615 (C. C. A. Tex.); instance, In re Gray, 21 A. B. R. 375, 170 Fed. 638 (D. C. Okla.); instance, *Reardon v. Rock Island Plow Co.*, 22 A. B. R. 26, 168 Fed. 654 (C. C. A. Ills.); *Franklin v. Stoughton Wagon Co.*, 22 A. B. R. 63, 168 Fed. 857 (C. C. A. Okla.); instance, reclamation refused, In re Agnew, 23 A. B. R. 360 (D. C. Miss.); In re Schneider, 29 A. B. R. 469, 203 Fed. 589 (D. C. Pa.); In re Boschelli, 25 A. B. R. 528, 183 Fed. 864 (D. C. Pa.); In re Forse and Roseboom, 25 A. B. R. 134, 182 Fed. 212 (D. C. N. Y.); In re Fred. A. Lausman, 25 A. B. R. 186, 183 Fed. 647 (D. C. Ky.); *Nat. Bank v.*

Carbondale Mach. Co. No. 2, 27 A. B. R. 850, 195 Fed. 180 (C. C. A. Kan.); *Colonial Trust Co. v. Thorpe*, 27 A. B. R. 451, 194 Fed. 390 (C. C. A. Va.); *Woods v. Brunswick, etc., Co.*, 27 A. B. R. 172, 190 Fed. 935 (C. C. A. Wash.); [Amendment of 1910 to Bankr. Act, § 47 (a) (2), held not retroactive] *Arctic, etc., Co. v. Armstrong Trust Co.*, 27 A. B. R. 562, 192 Fed. 114 (C. C. A. Pa.); *Nauman Co. v. Bradshaw*, 27 A. B. R. 565, 193 Fed. 350 (C. C. A. Ia.).

Trustee Using Property Held on Conditional Sale, Pending Litigation over Its Title.—It is held that where the trustee uses property, such as machinery, during the continuance of the bankrupt's business under order of the court, pending which certain reclamation proceedings were being carried on, the conditional vendor cannot charge the trustee with the "rental" for such use, unless the vendor take some positive step, such as by order of the court, that will appraise the trustee of the contemplated charge, In re Datterson Pub. Co., 26 A. B. R. 582, 188 Fed. 64 (C. C. A. Pa.), quoted at § 2035½.

to the terms of the contract and notes exhibited with the intervening petition."

John Deere Plow Co. v. Anderson, 23 A. B. R. 480, 174 Fed. 815 (C. C. A. Ga.): "The trustee has no greater right in property sold under a conditional sale contract than the bankrupt had. * * * In this case the sale was undoubtedly valid as between the parties, and the plow company was therefore entitled to the property as against the trustee."

Obiter, *In re Great Western Mfg. Co.*, 18 A. B. R. 261, 152 Fed. 123 (C. C. A. Neb.): "The vendor had the right to take the machinery and material out of the mill and dispose of it as it saw fit. If it had applied to the court to do so and its application had been denied, it would have been entitled to recover of the trustee the value of its right."

Or the proceeds of such property if the same are traceable into the trustee's hands,⁴⁷ especially where such proceeds were to be held in trust for the seller.⁴⁸ But such property is not reclaimable where it would not be reclaimable under state law,⁴⁹ as laid down by the highest tribunal of the state;⁵⁰ as, for instance, where it is in reality an absolute sale disguised as one on condition.⁵¹

But the conditional seller need not always assert his rights by way of reclaiming the property in kind, for, in most states, he may have the property sold and the proceeds applied on the balance of the purchase price, on the theory of equitable lien.^{51a}

In re Max Goldman, 23 A. B. R. 497, 174 Fed. 579 (C. C. A. Ohio): "In equity the reserved title of the vendor is regarded as in the nature of

⁴⁷. *In re Fabian*, 18 A. B. R. 488, 151 Fed. 949 (D. C. Pa.); compare, § 1882; instance, looms sold on conditional sale, *Davis v. Crompton*, 20 A. B. R. 53, 158 Fed. 735 (C. C. A. Pa.); instance, steel rails, *Nat. Bank v. Williams*, 20 A. B. R. 79, 159 Fed. 615 (C. C. A. Tex.); instance, obiter, "corn popper," *In re Grainger*, 20 A. B. R. 166, 173, 160 Fed. 69 (C. C. A. Calif.); *In re Lutz*, 28 A. B. R. 649, 197 Fed. 492 (D. C. Ark.).

⁴⁸. *In re McGehee*, 21 A. B. R. 656, 166 Fed. 928 (D. C. Ga.).

⁴⁹. *In re Burke*, 22 A. B. R. 69, 168 Fed. 994 (D. C. Ga.); *Liquid Carbonic Co. v. Quick*, 25 A. B. R. 394, 182 Fed. 603 (C. C. A. Pa.).

⁵⁰. *In re Burke*, 22 A. B. R. 69, 168 Fed. 994 (D. C. Ga.).

⁵¹. Compare instances, ante, § 1228; *In re Rinker*, 23 A. B. R. 62, 174 Fed. 490 (D. C. Pa.).

^{51a}. **Statute Requiring Refund on Taking Possession, Not Applicable When Property Sold Rather than Reclaimed.**—In the event that the conditional seller does not petition for reclamation but asks the court to pay him from the proceeds, a statute requiring refund on taking possession will not be applicable. *In re Max*

Goldman, 23 A. B. R. 497, 174 Fed. 579 (C. C. A. Ohio): "It does not provide a remedy which is precisely according to the principles of equity, for it is provided that the refunding by the vendor shall not be required unless the amount he has received exceeds 25 per cent. of the contract price. If the vendor, instead of taking back the property, should foreclose the vendee's right by a proceeding in equity, there would be no such limitation. On the other hand, as the law then stood, the vendor, treating the title of the property reserved by the contract as a security for the payment of the price, might file his bill in equity to obtain a judicial sale of the property and an appropriation of the proceeds to the payment of the debt. By the latter course the equity of the vendee was protected by the conscience of the court and its power of control over the sale. He suffered no wrong of which he could complain. That the vendor has the right to proceed in this manner, we think, cannot be doubted. It is a favorite jurisdiction of equity to relieve against forfeitures, and the practice of this remedy will subserve the purposes of justice in such cases."

a security for the payment of the price, and in some States it is held that such a conditional sale is the equivalent of an out and out sale and a mortgage back to secure the payment of the purchase money. At law the transfer of the property gives to the vendee the right to the possession so long as he is performing his agreement to pay. But, when he fails to do this, his right to the possession ceases, and he then holds it for the vendor. But in equity these considerations are regarded as technical merely, and the court will look to see whether the vendor has such a hold or claim upon the property as entitles him to subject it to the payment of the purchase money. The maxim that equity follows the law is inapt where the legal remedy is inadequate to the enforcement of equitable rights. 16 Cyc. 137. There are many instances in the law of sales where even at the common law a lien is implied for the protection of the vendor in cases of ordinary sales. Although the agreement is perfected so as to pass the title for most purposes, still the vendor is allowed a lien for the price, while it remains in his own possession; or where he has delivered it to a common carrier according to agreement and the carrier is held to be the agent of the vendee for the purpose of accepting delivery, the vendor is allowed the privilege of recaption in transitu if the vendee becomes insolvent or becomes bankrupt, and in equity the vendor of real property is given a lien, a claim, a hold upon it, notwithstanding it has gone into the possession of the vendee, and no agreement for a lien has been made."

Proceedings for reclamation, however, are equitable; and, consequently, the owner may be directed, as a condition precedent to the recovery of the property, to return the payments received by him on account of the purchase price, less suitable allowances for its use, depreciation, etc., where, under the local law, such payments might have been recovered by an independent action.⁵²

§ 1879. Of Goods Bought under Misrepresentation or While Grossly Insolvent.—Thus, goods may be reclaimed that have been procured through the misrepresentations of the buyer as to his financial condition or by other fraud, or (in some states) under such circumstances of hopeless insolvency as to have precluded any intention to pay and where there was therefore no meeting of minds and no passing of title.⁵³

Thus, as to sales on misrepresentation as to financial condition, reclamation has, on the facts, sometimes been granted.⁵⁴

In *re Hamilton Furn. & Carpet Co.*, 9 A. B. R. 65, 117 Fed. 774 (D. C. Ind.): "This is but a modern application of that ancient doctrine that where a party,

⁵². In *re Hooven-Owens-Reutschler Co.*, 28 A. B. R. 135, 195 Fed. 424 (C. C. A. Mich.).

⁵³. *Halsey v. Diamond Distilleries Co.*, 27 A. B. R. 333, 191 Fed. 498 (C. C. A. Pa.); In *re Spann*, 25 A. B. R. 551, 183 Fed. 819 (D. C. Ga.); In *re Russell & Birkett*, 5 A. B. R. 608 (Ref. N. Y.). Compare § 1169, right to rescind for fraud unaffected.

⁵⁴. In *re Patterson & Co.*, 10 A. B. R. 748, 125 Fed. 562 (D. C. Tex.); In

re Weil, 7 A. B. R. 90, 111 Fed. 897 (D. C. N. Y.); In *re Bendall*, 25 A. B. R. 698, 183 Fed. 816 (D. C. Ala.); In *re Appel Suit & Cloak Co.*, 28 A. B. R. 818, 198 Fed. 322 (D. C. Colo.). Compare, where rescission and seizure on replevin occurred before bankruptcy court took possession, under the doctrine enunciated at § 1585, ante, *William Openhym & Sons v. Blake*, 19 A. B. R. 639, 157 Fed. 536 (C. C. A. Mo.), quoted at § 1585.

by false representations as to his solvency, knowingly made, induces the owner of goods, who, in ignorance of their falsity relies upon such representations, to sell them, he is entitled to disaffirm the contract and recover the goods. Fraud renders all contracts voidable *ab initio*, both at law and in equity. No man is bound by a bargain into which he has been deceived by fraud, because assent is necessary to a valid contract, and there is no real assent where fraud and deception have been used as instruments to control the will and induce the assent."

In *re Marco Gany*, 4 A. B. R. 576, 103 Fed. 930 (D. C. N. Y.): "It is not necessary that the false representations should be the sole and exclusive consideration for the credit; but only that they were a material consideration, without which in all probability the credit would not have been given."

Compare, analogously (plenary action in State Court), *Silvey & Co. v. Tift*, 17 A. B. R. 20, 123 Ga. 804: "If one purchasing goods makes a false representation as to a material matter, and the owner of the goods relies on such statement and sells upon discovering the fraud the owner may rescind and reclaim his property, or so much of it as is still in the possession of the purchaser."

And reclamation has sometimes been refused because the proof was insufficient;⁵⁵ or because there was no tender back of the consideration received.⁵⁶

In *re Murphy Barbee Shoe Co.*, 11 A. B. R. 434 (Ref. Mo.): "In order to make a complete rescission of an executed contract of sale by a vendor, it is necessary for him to tender to the vendee all of value received by him from the vendee. The parties must all be placed in *statu quo*."

Reclamation also has been refused where it was doubtful whether there was any reliance on the false statement, the seller admitting he would have sold anyway, and the making of the false assertion that the buyer had two dollars for every one he owed being denied by the bankrupt.⁵⁷ Likewise, it has been refused where the seller knew the buyer was in failing circumstances, and was unreliable in his statements as to financial condition.⁵⁸ Where there was no reliance on a false statement made to a commercial agency, the mere fact that it was made will not entitle the seller to reclaim.⁵⁹

But reliance may be proved by circumstantial evidence and the mere facts that the statement was asked for and given as a basis of credit and that the goods were supplied within a reasonable time thereafter are sufficient proof that the creditor parted with the merchandise on the strength of the representation, if it be not overcome by adequate rebutting evidence.⁶⁰

55. In *re Rose*, 14 A. B. R. 345 (D. C. Penn.); *Levi v. Picard*, 17 A. B. R. 430, 148 Fed. 654 (D. C. N. Y.); In *re American Knit Goods Mfg. Co.*, 19 A. B. R. 212, 155 Fed. 906 (D. C. N. Y.); In *re Isaac Berg*, 25 A. B. R. 170 (Ref. Mass.); In *re Sol. Aarons & Co.*, 28 A. B. R. 399, 193 Fed. 646 (C. C. A. N. Y.); In *re Marengo, etc., Co.*, 29 A. B. R. 46, 199 Fed. 474 (D. C. Ala.).

56. Compare, *obiter*, to same effect, *Silvey & Co. v. Tift*, 17 A. B. R. 20, 123 Ga. 804.

57. In *re Davis*, 7 A. B. R. 276, 112 Fed. 294 (D. C. N. Y.).

58. In *re Sweeney*, 21 A. B. R. 866, 168 Fed. 612 (C. C. A. Tenn.).

59. In *re Epstein*, 6 A. B. R. 60, 109 Fed. 878 (D. C. Ark.); In *re Roalswick*, 6 A. B. R. 752, 110 Fed. 639 (D. C. Mont.).

60. In *re Reed*, 26 A. B. R. 286, 191 Fed. 920 (D. C. Okla.), quoted at § 2569.

And intention to deceive must exist in order to entitle to reclamation on the ground of misrepresentation.⁶¹ But it is not essential to prove that the intention was not to pay.⁶² Reclamation has been refused where the untrue statement was incomplete rather than false;⁶³ where the creditor's salesman read off from the printed forms a long list of questions and took down the bankrupt's answers thereto, omitting some, instead of submitting the printed form for the bankrupt to act on in his own way.⁶⁴ Reclamation will be refused where, notwithstanding fraud on the part of the bankrupt, the seller has affirmed the sale by some act on his part.⁶⁵ And merely that the bankrupt had failed to pay for the property bought by him shortly before bankruptcy would not warrant its recovery in reclamation proceedings.⁶⁶

Where there have been sales on other frauds, reclamation has sometimes been granted;⁶⁷ and sometimes been refused.⁶⁸

Thus, where a buyer mortgaged or assigned all its assets between the time of giving its order and the time of the delivery of the goods, rescission and reclamation have been allowed, the facts indicating design.⁶⁹

In some states the rule prevails that where goods have been sold at a time when the buyer knew he was so hopelessly insolvent that he could have had no reasonable prospect of being able to pay for them and so no real meeting of mind between the parties could be held ever to have taken place and no title ever to have passed, such apparent sale may be rescinded and the goods recovered. This rule does not appear to prevail in Pennsylvania,⁷⁰ however; but apparently does prevail in New York.⁷¹ It also prevails in Ohio⁷² and in Iowa.⁷³

Gillespie v. Piles, 24 A. B. R. 502, 178 Fed. 886 (C. C. A. Iowa): "A vendor, who sells personal property to an insolvent vendee, who at the time he buys does not intend to pay for it, may rescind the sale and recover the property or its proceeds from any one but an innocent purchaser, and neither a re-

61. *In re Russell & Birkett*, 5 A. B. R. 608 (Ref. N. Y.). Analogously, *Lumber Co. v. Taylor*, 14 A. B. R. 231, 137 Fed. 321 (C. C. A. Pa.).

62. *Obiter*, *Ellet-Kendall Shoe Co. v. Ward*, 26 A. B. R. 114, 187 Fed. 982 (C. C. A. Oklahoma).

63. *Ellet-Kendall Shoe Co. v. Ward*, 26 A. B. R. 114, 187 Fed. 982 (C. C. A. Oklahoma).

64. *Ellet-Kendall Shoe Co. v. Ward*, 26 A. B. R. 114, 187 Fed. 982 (C. C. A. Oklahoma).

65. *Fowler v. Britt-Carson Shoe Co.*, 27 A. B. R. 232 (Sup. Ct. Ga.).

66. *Kellogg, etc., Co. v. Curtice*, 28 A. B. R. 906 (Ct. App. Mo.), *replevin suit*.

67. *Bloomington v. Empire Rubber Mfg. Co.*, 8 A. B. R. 74, 114 Fed. 1016 (D. C. N. Y.).

68. *In re O'Connor*, 7 A. B. R. 428,

112 Fed. 666 (D. C. Ga.): But the opinion in this case was obiter, for, in fact, the court found that a general scheme to defraud, which was the basis of the proceedings, had not been proven. It does not seem to state a proper rule anyway.

69. *Haywood Co. v. Pittsburgh Industrial Iron Works*, 19 A. B. R. 780, 163 Fed. 799 (D. C. Pa.).

70. *In re Lewis*, 10 A. B. R. 741, 125 Fed. 143 (D. C. Penn.). However, see *Lumber Co. v. Taylor*, 14 A. B. R. 231, 137 Fed. 321 (C. C. A. Penn.); *In re Murphy-Barbee Shoe Co.*, 11 A. B. R. 428 (Ref. Mo.).

71. *In re Levi & Picard*, 16 A. B. R. 756, 148 Fed. 654 (D. C. N. Y.).

72. *Talcott v. Henderson*, 31 Ohio State 162.

73. *Gillespie v. Piles*, 24 A. B. R. 502, 178 Fed. 886 (C. C. A. Iowa).

ceiver nor a trustee in bankruptcy is such a purchaser. A decisive question in the case therefore is: Did Hough intend to pay for these hogs when he bought them. * * * Hough had then been insolvent, and had been aware of that fact for many months. * * *

"It is contended, and it is conceded, that the insolvency of a purchaser does not prove his intent not to pay for the goods which he buys. Many an insolvent obtains goods on credit with the honest intent to pay for them, and many times he succeeds in doing so. * * *

"But he was not in the same financial or mental condition when he purchased of the interveners that he had occupied when he bought of earlier vendors. When he made the earlier purchases he had a reasonable expectation that he could pay for the hogs he purchased with the proceeds of hogs of later vendors in the way in which he had paid for other purchases for months. But, when he bought of the interveners he knew that he had no money or credit with which to pay for their hogs, that the only way in which he could pay for them was by the purchase and the sale of the hogs of subsequent vendors and the appropriation of the proceeds of these later purchases through the bank to the payment of the interveners, and he knew that he could not pay for them in that way because subsequent vendors would not sell to him after his known failure, and the bank would not take his drafts or honor his checks. In this state of the case it is incredible that he intended to pay for these hogs when he bought them. He knew it was impossible for him to pay for them, and the human mind is so constituted that it cannot harbor a serious intent that the being it directs shall do that which it knows it is impossible for it to accomplish. An insolvent buyer, who knows at the time of his purchase that his financial condition is such that it is and will be impossible for him to pay for his purchases, is conclusively presumed to have bought them with an intention not to pay for them; and a persuasive legal presumption to that effect arises from the fact that such a purchaser's affairs were in such a condition at the time of the purchase of the property that he could then have had no reasonable expectation of paying for it."

Of course, however, proof of mere insolvency is not sufficient.⁷⁴

The buyer's omission to disclose his insolvency to the seller is not fraudulent in law.⁷⁵

Strict proof seems to be required of the reclaimer where the ground urged is fraudulent misrepresentation.⁷⁶ And where the rule prevails, it depends upon the condition and intentions of the buyer at the time the contract of sale was entered into, not at the time of the delivery of the goods.

In *re Levi & Picard*, 16 A. B. R. 756 (D. C. N. Y.): "The right of the petitioners to reclaim the goods so delivered is based upon the proposition that if at the time of the receipt or delivery thereof, the vendees had reasonable cause to believe that they were unable to pay for them, and did not then intend to pay for them, the sale may be rescinded and the goods recovered, even though no such cause to believe or intent not to pay, can be proven or inferred as of the date of the sale.

⁷⁴. *Gillespie v. Piles*, 24 A. B. R. 502, 178 Fed. 886 (C. C. A. Iowa), quoted *supra*.

⁷⁵. In *re Davis*, 7 A. B. R. 276, 112 Fed. 294, 295 (D. C. N. Y.).

⁷⁶. In *re Murphy-Barbee Shoe Co.*, 11 A. B. R. 428 (Ref. Mo.); *Levi v. Picard*, 17 A. B. R. 431, 148 Fed. 654 (D. C. N. Y.).

"The refinement upon the well-established rule regarding rescission is not, in my opinion, sustained by authority or reason.

"*Donaldson v. Farwell*, 93 U. S. 631, is binding authority in this court. It was there held to be established that what entitles the vendee to disaffirm a contract of sale and recover his goods consists in the vendee's inducing the vendor 'to sell him goods on credit' when he was (a) insolvent, (b) concealed his insolvency, and (c) did not intend to pay for what he bought.

"Here the contract of sale was complete when the minds of the parties met on August 31st; and at that time, although the bankrupt firm was insolvent, there is no evidence that the partners knew that fact, and there is a plain inference that they then intended to pay for what they bought. * * *

"In practice, the petitioner's demand is especially vicious in bankruptcy. It is notorious that mercantile contracts for future deliveries, often many months distant, or extending over a long period of time, are the rule rather than the exception.

"That a contract for 'spring delivery' made in perfect honesty in October, may be avoided because an expert investigation after bankruptcy in May renders it probable or certain that when goods were delivered in April the vendee was insolvent, and therefore should have imputed to him an intent not to pay, contemporaneous with delivery, is intolerable. Such proceedings would render every mercantile failure a mockery to creditors who had given no credit or sold on short time, yet to this extent would the doctrine contended for lead the court."

The right of rescission is lost if the goods become a component part of a structure, not separable therefrom without manifest injury.⁷⁷

Reclamation will be refused where the property was not in the hands of the trustee but in the hands of the bankrupt, and the reclaimer had waited until the trustee had procured a summary order upon the bankrupt for surrender.⁷⁸

The right of reclamation is lost, of course, if the seller proves his claim as a creditor.⁷⁹

Amendment of 1910.—The Amendment of 1910 to Bankruptcy Act, § 47a (2), endowing the trustee with the attributes of a creditor "armed with process" does not, in general, cut off the right to reclaim property belonging to third parties.⁸⁰

In *re Gold*, 31 A. B. R. 18, 210 Fed. 410 (C. C. A. Ills.): "The vendors having at the earliest opportunity rescinded the sale, the title to the furs in ques-

77. *Lumber Co. v. Taylor*, 14 A. B. R. 231, 137 Fed. 321 (C. C. A. Penn.).

78. In *re Eliowich*, 17 A. B. R. 419, 148 Fed. 464 (D. C. N. Y.).

Pleading and Practice:

(a) Claimant must state the facts wherein the falsity consists. *Lumber Co. v. Taylor*, 14 A. B. R. 231, 137 Fed. 321 (C. C. A. Penn.).

(b) Claimant must state the debtor's intent to deceive. *Lumber Co. v. Taylor*, 14 A. B. R. 231, 137 Fed. 321 (C. C. A. Penn.); inferentially, In *re Russell & Birkett*, 5 A. B. R. 608 (Ref. N. Y.).

79. Compare, ante, § 639; also see *Lynch v. Bronson*, 20 A. B. R. 409, 160 Fed. 139 (D. C. Conn.), quoted at § 639.

80. But compare, In *re Whatley Brothers*, 29 A. B. R. 64, 199 Fed. 326 (D. C. Ga.), wherein the court seems to construe a Georgia decision controlling the case as holding that the reclamation would be refused not only as against an innocent purchaser for value, but also as against a creditor holding a lien, although the decision itself would seem to have implied that the lien must likewise be given for value.

tion never passed to the bankrupt, by reason of her fraudulent representations to the vendors, therefore the trustee took no title thereto inasmuch as, under the laws of Illinois, as construed by the courts of the State, the rights of the defrauded vendor prevailed over the claims 'of a creditor holding a lien by legal or equitable proceedings thereon.'"

In re [Appel] Suit & Clock Co., 28 A. B. R. 818, 198 Fed. 322 (D. C. Colo.): "The Amendment to § 47 of the bankruptcy act does not attempt to put the trustee in such a favored position [purchaser for value]. It only gives him 'the rights, remedies, and powers of a creditor holding a lien.' Prior to the amendment the trustee would have taken title to these mortgages, subject to the claimants equities, i. e., a right to rescind the sale induced by the vendee's fraud. It must, therefore, be held that in this jurisdiction, said amendment does not cut off the right of petitioners to rescind the sale and reclaim the unsold part of his goods."

§ 1879¹/₄. Election to Rescind.—If the transferrer elects to rescind he must proceed promptly, and after having made his election, he will be bound.⁸¹

In re Kenyon, 19 A. B. R. 194, 156 Fed. 863 (D. C. Ohio): "Having made proof of his claim and secured its allowance, he is, in the absence of inadvertence, fraud or mistake, none of which are alleged, bound thereby, because when a creditor makes proof of his claim against a bankrupt's estate, he stands in the position of a plaintiff at law and becomes a party to the suit."

Varnish Works v. Haydock, 16 A. B. R. 286, 143 Fed. 318 (C. C. A.): "As the referee properly said in his opinion, it was open to the petitioner, the purchase having been procured by fraud, to elect whether to confirm the sale notwithstanding, and maintain the position of a creditor for the price, or to repudiate the sale and recover the goods. But the vendor must make his election promptly on discovery of the fraud. This is the settled law. Upon this principle Judge Ray held in In re Hildebrandt, 10 Am. B. R. 184, 120 Fed. 992, that a vendor could not affirm the contract of sale as to part of the goods, and claim the price and disaffirm as to another part, and recover the goods in specie. And see Seavey v. Potter, 121 Mass. 297. And having made his election in such circumstances, the vendor makes it once for all. Kennedy v. Thorp, 51 N. Y. 174; Moller v. Tuska, 87 N. Y. 166; Heller v. Elliott, 44 N. J. L. 467; Carter v. Smith, 23 Wis. 497. The petition did not state when the petitioner became aware of the falsity of the bankrupt's representations of its solvency and of its fraudulent purpose, or whether it was before or after the petitioner proved its claim and participated in the proceedings as a creditor. And if, as it has in some cases been held, the burden of proof that the election was made with knowledge of the facts is upon the party who urges the estoppel, it would be difficult to resist the conviction that the circumstances attending the assignment and the adjudication of bankruptcy were sufficient to have shown the petitioner that the bankrupt in procuring the goods had made false representations in regard to its sol-

81. Compare ante, § 639; compare, analogously, to same effect, Thomas v. Sugerman, 19 A. B. R. 509, 157 Fed. 669 (C. C. A. N. Y.); instance, perhaps, Lynch v. Bronson, 20 A. B. R. 409, 160 Fed. 139 (D. C. Conn.), quoted at § 639.

Proof of Claim as Unsecured Debt, Not Waiver of "Vendor's Privilege" to Reclaim in Louisiana.—Sessler v. Paducah Distilleries Co., 21 A. B. R. 723, 168 Fed. 44 (C. C. A. La.).

vency. Not only did the petition make no claim that the petitioner was ignorant, at the time of proving its claim, of the facts in regard to the representations of the bankrupt and of its intention in making the purchase, but the facts stated by the referee are sufficient, *prima facie*, to support the conclusion that the petitioner had knowledge of the essential facts when it voted for the trustee. In these circumstances, the election of the petitioner to prove its claim as a general creditor was final. There is good ground for saying that it was too late for the exercise of an election after the petitioner had joined the general creditors in shaping and carrying forward the bankruptcy proceedings and influencing their associates in their action. The suggestion that the proceedings probably would have been the same without the petitioner's co-operation cannot avail. The assumption of the position of a general creditor toward the assets would naturally be a strong inducement to the other creditors in pursuing the bankruptcy proceedings, for this would imply a sharing of the assets, and this result would be defeated if their associates were permitted to turn about and reclaim the assets in specie."

Similarly, where funds have been converted, there arises a right of election either to follow the proceeds or to treat the conversion as a debt; and where the injured party accepts a transfer of other property for the converted property, he will be held to have elected to treat the conversion as a debt, in which case the transfer may be a preference.⁸²

Under the law of some states the right to rescind a sale and reclaim the property on the ground of fraud is lost not only where the goods have gone into the possession of an innocent purchaser for a valuable consideration, but also where one, for a valuable consideration, has acquired a lien thereon; thus, by statute, in Georgia.⁸³

And it has been held, in such states, that the trustee in bankruptcy, because of the lien creditor's rights conferred upon him by the amendment of 1910 to § 47a (2), cannot be compelled to surrender property in his possession, even though the vendor could have successfully reclaimed it as against the bankrupt on the ground of fraud.

In *re Whatley Bros.*, 29 A. B. R. 64, 199 Fed. 326 (D. C. Ga.): "While the courts are not in entire accord, I think it may be considered as settled now that the purpose of the act of June, 1910, was to give the trustee in bankruptcy a lien for the benefit of creditors generally, such as a creditor would have 'by legal or equitable proceedings.' Such is the plain language of the amendment, and there is no escape, so far as I can see, from the conclusion that this was the intent of Congress in its enactment. It is recognized, of course, that the main purpose of the amendatory act of 1910 was to relieve general creditors from the situation which had been created by many decisions, notably by the decision in the *York Manufacturing Company Case*, 201 U. S. 344, 15 Am. B. R. 633, 26 Sup. Ct. 481, 50 L. Ed. 782, by which the liens of unrecorded mortgages and conditional bills of sale, which, under the State laws, would be good as between the parties, were held as good against the bankrupt estate. But, though probably having this particular purpose more distinctly in mind, Congress gave to trustees in bankruptcy this lien, which

⁸². Compare, analogously, *Atherton v. Green*, 24 A. B. R. 650, 179 Fed. 806 (C. C. A. Ills.), quoted at § 1307½. ⁸³. In *re Whatley Bros.*, 29 A. B. R. 64, 199 Fed. 326 (D. C. Ga.).

operates generally and which attaches to all property coming into the custody of the bankruptcy court.

"It has the same effect as a judgment at law or in equity."

§ 1879 $\frac{1}{2}$. **Delay in Rescission.**—In bankruptcy the usual rules prevail as to the necessity for diligence in rescission and of putting the parties in statu quo.

Compare [William] Openhym & Sons *v.* Blake, 19 A. B. R. 639, 157 Fed. 536 (C. C. A. Mo.): "We do not think appellants should be denied relief because they delayed intervening in the bankruptcy court until after a partial dividend was declared. The fraud was practiced on appellants and the goods obtained July 13th, the sale was rescinded August 21st, and the intervening petition was filed in the bankruptcy court December 21st. At all times after the rescission of the sale the purpose of appellants to rely thereon was manifest. They were fairly diligent in the assertion of their rights, and no one seems to have been prejudiced by the short delay that occurred. That the filing of the intervening petition was delayed until after the dividend injured no one. The trustee and the court were aware that appellants had rescinded the sale, and the dividend took but a part of the funds on hand. There remained more than enough to pay the appellants, and had the intervening petition been presented and allowed much earlier the same dividend would probably have been declared. At least no reason appears why it should not have been."

§ 1879 $\frac{3}{4}$. **Subrogation to Right of Reclamation.**—Where a surety has paid the claim afterwards, or it has been assigned, the surety or assignee may be subrogated to the right of reclamation.⁸⁴

Sessler *v.* Paducah Distilleries Co., 21 A. B. R. 723, 168 Fed. 44 (C. C. A. La.): "* * * it is also contended that, as Menard Bros. took no express subrogation at the time of payment, they acquired no rights of the original creditor to rescind the sale. There may be some doubt as to whether any subrogation took place by contract; but as Menard Bros. were sureties * * * and paid the debt, we think they are legally subrogated under the Louisiana Code. * * * We have no doubt about the right of a surety to prosecute his claim in bankruptcy in the name of the principal creditor, when subrogation takes place after proof of debt."

§ 1880. **Reclaiming Part Still in Trustee's Hands, Proving Claim for Balance.**—Where part of the goods have been sold and the proceeds are no longer traceable, the weight of authority seems to be that the seller may reclaim the part still in specie and make proof of debt on an implied contract for the balance sold, and that the two claims are not inconsistent and that no election need be made;⁸⁵ although, on reason, it would seem that such course would amount to affirming and denying contractual relations at the same time.⁸⁶

However, the distinction seems to be that so long as the original con-

⁸⁴ L. A. Becker Co. *v.* Gill, 30 A. B. R. 429, 206 Fed. 36 (C. C. A. Mo.).

⁸⁵ In re Hirschman, 4 A. B. R. 715, 104 Fed. 69 (D. C. Utah); In re Hilbrandt, 10 A. B. R. 184, 120 Fed. 992

(D. C. N. Y.); Silvey & Co. *v.* Tift, 17 A. B. R. 21, 123 Ga. 804; ante, § 638.

⁸⁶ Compare discussion, ante, § 638.

tract of sale is not affirmed, but that what is affirmed is only the implied contract to pay for goods converted, as if bought, there is no inconsistency.⁸⁷

§ 1881. Goods Stopped in Transitu.—Goods may be reclaimed where the right of stoppage in transitu existed and was duly exercised but delivery was made notwithstanding. The right of stoppage in transitu is lost if the goods reach the actual possession of the bankrupt or his agent or his trustee⁸⁸ at the designated terminus and the same rule has been held to govern when they have reached the possession of the receiver, even though the goods were shipped after the consignee had gone into bankruptcy;⁸⁹ though as to goods shipped after bankruptcy, doubtless title ordinarily would not pass, for other reasons;⁹⁰ moreover, the custody of the receiver differs from that of the trustee for the latter is an "owner" have title, by Bankr. Act, § 70 (a), whilst the receiver is a mere custodian.⁹¹ Seizure or interception before the goods have reached their destination,⁹² however, will not end the right of stoppage in transitu, nor will it be ended where the trustee or receiver has induced the carrier to deliver.

But notice to the carrier must be timely, and if it is not given to the particular agent in charge, it must be given to the principal in time for the latter to stop the delivery.

In re White, 29 A. B. R. 358, 205 Fed. 393 (D. C. Pa.): "It has often been held that when the goods are in the custody of the servant or agent notice to the principal must be in time by use of reasonable diligence to prevent the delivery to the vendee. While it may be said that this has generally been applied to contests between consignor and carrier, it nevertheless serves to indicate that notice to the principal not in immediate possession of the goods is not to be regarded as in itself sufficient. The notice must be communicated to the person in charge or served on the principal in time to permit of such. Something more remains to be done. To hold otherwise would, indeed, entail great hardship upon carriers, involving them often in loss and rendering their duties precarious, thereby necessarily impeding the dispatch of business.

"The carrier was requested by the shipper, through letter addressed to the Duquesne Freight Station at Pittsburgh, to stop delivery of the goods at Williamsport. The letter reached its destination at Pittsburgh upon the day the receiver made his demand upon the agent at Williamsport, possibly an hour or so before. Was this sufficient to justify stoppage at Williamsport when delivery was refused? I think not, the agent at Williamsport had not then, and in fact for several days thereafter, did not have any knowledge of the request made of

87. *Silvey & Co. v. Tift*, 17 A. B. R. 21, 123 Ga. 804; In re Heinsfurter, 3 A. B. R. 113, 97 Fed. 198 (D. C. Iowa). See ante, § 638.

88. *A fortiori* (delivery to receiver). In re Allen, 24 A. B. R. 574, 178 Fed. 879 (D. C. Pa.), quoted at § 1168; also compare, to same effect, *Millard v. Webster*, 54 Conn. 415; also compare, *McElroy v. Seery*, 61 Md. 389; also compare (Eng.) *Scott v. Pettit*, 3 Bos.

& S. 469; (Eng.) *Inglis v. Usherwood*, 1 East 515.

89. Compare ante, § 1166.

90. *Jenks v. Fulmer*, 160 Pa. St. 527; *Harris v. Tenney*, 85 Tex. 254.

91. Compare ante, § 1879.

92. Delivery to mere "messenger" held not sufficient to terminate right. *Tufts v. Sylvester*, 70 Me. 213, 1 Am. State Rep. 303.

the carrier. His refusal was not based on the consignors' demand to stop delivery, it was in pursuance of the rule of the company not to deliver when the property of consignee of goods is, to their knowledge, under levy by sheriff's execution. The refusal by the agent therefore being unwarranted, possession passed to the receiver and title vested."

§ 1882. Converted Property or Its Traced Proceeds, Reclaimable.—Property converted by the bankrupt may be recovered; so may its proceeds if they can be identified and traced;⁹³ but if neither the property itself nor its proceeds can be identified, the fact that it was converted will not entitle its owner to priority of payment out of the estate: the owner will simply have the right to waive the tort and present his claim as on contract for the value of the goods converted and pray to be allowed to share in the dividends.⁹⁴

Thomas v. Taggart, 209 U. S. 385, 19 A. B. R. 710: "The rule is generally recognized that if the title to property claimed is good as against the bankrupt and his creditors at the time the trustee's title accrued, the title does not pass and the property should be restored to its true owner; or, if the property has been sold, the proceeds of the sale take the place of the property."

In *re Mulligan*, 9 A. B. R. 11, 116 Fed. 715 (D. C. Mass.): "On the other hand, the mere misapplication of trust funds does not create in favor of the defrauded beneficiary a claim upon the general estate of the defrauding trustee superior to that of his general creditors. There are some cases, indeed, which give to the beneficiary a general priority or something very near it; but they are opposed to the great weight of authority. Other cases do not give to the defrauded beneficiary, merely as such, a general priority, yet allow him a prior charge upon the general assets of the defrauded trustee, where it is shown that the trust fund has been absorbed in the trustee's business or general estate, though it cannot be followed into any specific property remaining. Some of these latter cases distinguish between a dissipation of the trust fund, as in the payment of the trustee's debts, and an employment of the fund in the purchase of property; but, if the purchased property cannot be traced, there would seem to be no material difference. It might be possible, indeed, to

^{93.} Compare, In *re Grainger*, 20 A. B. R. 166, 160 Fed. 69 (C. C. A. Calif.); compare, analogously, where order is on third person, In *re Rose Shoe Mfg. Co.*, 21 A. B. R. 725, 168 Fed. 39 (C. C. A. N. Y.).

^{94.} In *re Neely*, 5 A. B. R. 836, 108 Fed. 371 (D. C. N. Y.); *Erie R. R. Co. v. Dial*, 15 A. B. R. 559, 140 Fed. 689 (C. C. A. Ohio), which was a case of conversion of goods sold C. O. D. taken from the carrier before payment, by the buyer and used in manufacture. See also, § 1883; In *re Dorr*, 21 A. B. R. 752 (Ref. Calif.); In *re Brunsing, Tolle & Postel*, 22 A. B. R. 129, 169 Fed. 668 (D. C. Calif.), quoted at § 1883; In *re Emerson, Marlow & Co.*, 29 A. B. R. 173, 199 Fed. 99, (C. C. A. Ill.); *obiter*, *Atherton v. Green*, 24 A. B. R. 650, 179 Fed. 806 (C. C. A. Ills.), quoted ante, § 1307.

Waiving Tort and Affirming Contractual Relations.—See ante, § 638. See also, *Thomas v. Taggart*, 19 A. B. R. 710, 209 U. S. 385, wherein the Supreme Court held that where the customer's proof of claim contained a reservation of whatever rights he had against the bankrupts of either of them, for or on account of their failure to return the stock covered by the receipt, he was not precluded after discovery that his shares of stock had been returned to the trustee in bankruptcy, from reclaiming them as his own property, though he had actively participated at the meetings held for the election of trustee. See also, In *re Berry*, 23 A. B. R. 27, 174 Fed. 409 (C. C. A.), growing out of the same bankruptcy.

require the general creditors of the defaulting trustee, in order to defeat the prior claim of the cestui upon any remaining property, to show affirmatively that the trust fund was not converted into the specific piece of property upon which the cestui seeks to enforce a lien; but to change the cestui's claim for priority into a mere shifting of the burden of proof, finds no considerable support in the decided cases."

Thus, converted shares of stock,⁹⁵ or the proceeds of converted shares of stock in a stockbroker's hands, where the relation between the stockbroker and his customer is held to be that of pledgee and pledgor or bailee and bailor rather than that of debtor and creditor, may be traced and recovered.⁹⁶

Again, the proceeds of goods sold to the bankrupt on conditional sale may be ordered surrendered, where the sale was valid as against the trustee

95. Instance, transfer by bankrupt stockbroker under forged powers of attorney, *Unity Banking & Sav. Co. v. Boyden*, 20 A. B. R. 264, 159 Fed. 916 (C. C. A. Ohio).

96. See ante, § 1313. Instance, *In re Bolling*, 17 A. B. R. 399 (D. C. Va.); *In re Berry & Co.*, 17 A. B. R. 467, 147 Fed. 208 (C. C. A. N. Y.); *Thomas v. Taggart*, 19 A. B. R. 710, 209 U. S. 385 (affirming *In re Berry & Co.*, 17 A. B. R. 467, 147 Fed. 208); analogously, *Richardson v. Shaw*, 19 A. B. R. 717, 209 U. S. 365; *In re (Fred) Dorr*, 21 A. B. R. 752 (Ref. Calif.); *In re Brown & Co.*, 22 A. B. R. 659, 171 Fed. 281 (D. C. N. Y.); compare, *In re Meadows, Williams & Co.*, 23 A. B. R. 124, 173 Fed. 694 (D. C. N. Y.), where were involved the rights of the parties where stock, paid for by a customer, was bought through a correspondent in another city, who retained the stock as security for the purchase price which the bankrupt never transmitted, the correspondent meanwhile also having a lien on the bankrupt's seat in a stock exchange to secure any unpaid balance between the two; also, see *Denison v. Emery*, 153 Fed. 427 (C. C., affirmed sub nom. *Harmon v. Sprague*, 163 Fed. 486), involving the rights of parties in much the same relation as in *Meadows, Williams & Co.*, supra; *In re A. O. Brown & Co.*, 25 A. B. R. 800, 183 Fed. 861 (D. C. N. Y.).

Stock Jointly Pledged with Other Stock as Collateral to Loan.—Where stock has been pledged jointly with other stock as collateral to a loan but the loan has been satisfied out of the other pledged stock, nevertheless it must contribute its share. *In re McIntyre & Co.*, 24 A. B. R. 626, 176 Fed. 552 (C. C. A. N. Y.).

Instance, where conversion held not

proved. *In re McIntyre & Co.*, 24 A. B. R. 1, 176 Fed. 552 (C. C. A. N. Y.): "The basis of the claimant's demand is the conversion of his stock. The only evidence tending to establish a conversion is the entries in the stock record book showing that upon one particular day there was a difference of only five shares between the receipts and deliveries of distillers stock. From this testimony the claimant seeks to draw the inference that on that day the brokers must have disposed of, and consequently, have converted his stock. But the testimony does not warrant the drawing of this inference. There is nothing to show that if the claimant had demanded his stock on the day in question he would not have received it. The entries do not show necessarily that the brokers did not have under their control sufficient shares to make delivery. They may, in regular course of business, have parted with the possession of as many shares as they received and yet have retained subject to their absolute control in the possession of another sufficient stock to meet the claimant's demand. If they did this there was no conversion."

Remedies Where Bankrupt Broker Has Converted Customer's Stock.—

Where a bankrupt broker has converted his customer's stock several remedies are open to the customer: (1) An action of tort for the conversion; (2) waiver of tort and suit for proceeds; (3) following of proceeds as trust fund; (4) breach of contract; (5) assumption on implied contract to refund the money paid, [partially, combining (2) and (3), as to which see ante, § 638], see *In re A. O. Brown*, 23 A. B. R. 423, 175 Fed. 769 (C. C. A. N. Y.).

and the proceeds are successfully traced.⁹⁷ Similarly, the converted proceeds of a collection of a note may be reclaimed if traceable, but may not be reclaimed if not traceable.⁹⁸

The right of reclamation is lost if the owner, or fraudulently induced seller, files his claim as a creditor.⁹⁹

In *re Berry*, 23 A. B. R. 27, 174 Fed. 409 (C. C. A.): "This is a petition to revise an order of the District Court affirming the report of a special master to the effect that the petitioner had elected to prove against the estate for the value of stock wrongfully hypothecated by the bankrupts, and therefore could not subsequently claim the stock or its profits specifically. It is to be inferred from the opinion of the Supreme Court in *Thomas v. Taggart*, 209 U. S. 385, 19 Am. B. R. 710, that a creditor, who does this without making any reservation has finally elected his remedy."

Unless the filing of the claim was made without knowledge of all the facts, or in ignorance of legal rights.¹ And the acceptance of a transfer of other property to make amends for the property converted is an election to treat the conversion as a debt and the transfer may constitute a preference.²

In *re McIntyre & Co.*, 24 A. B. R. 626, 176 Fed. 552 (C. C. A. N. Y.): "* * * the identity of which has at no time been lost; the certificate No. 10,277, which the trustees now hold, is the very same one which he entrusted to McIntyre & Co. on March 14, 1908. The stock was deposited with McIntyre & Co. merely as security to protect them against any losses from transactions on the market for Pippey's account. The firm had no right to pledge them for any of its own debts. When it did pledge them to the trust company, the day before its failure, the firm had no transaction pending and was itself indebted to Pippey. This was a larceny of his stock, *Tompkins v. Morton Trust Co.*, 91 App. Div. 274; *Kavanaugh v. McIntyre*, 21 Am. B. R. 327; 128 App. Div. 722; no one disputes that proposition."

Obiter, In *re Berry*, 23 A. B. R. 27, 174 Fed. 409 (C. C. A.): "If the record in this matter showed that the petitioner made his claim without knowledge of all the facts, or even in ignorance of his legal rights to follow the certificates or their proceeds, the situation might be different, but it does not. On the contrary, the special master and the district judge both found that he acted with full knowledge of all the facts. The situation he is now in is not due to his laches or to any estoppel arising out of anything done to the prejudice of others, but to the fact that he has deliberately elected a remedy inconsistent with the claim he now makes."

A fortiori, certificates of stock, bought and paid for by a customer be-

97. In *re Fabian*, 18 A. B. R. 488, 151 Fed. 949 (D. C. Pa.).

98. Obiter, *Atherton v. Green*, 24 A. B. R. 650, 179 Fed. 806 (C. C. A. Ills.), quoted ante, at § 1307½.

99. Compare discussion ante, § 639; also see *Lynch v. Bronson*, 20 A. B. R. 409, 160 Fed. 139 (D. C. Conn.), quoted at § 639; but compare, analogously, *Sessler v. Paducah Distilleries Co.*, 21

A. B. R. 723, 168 Fed. 44 (C. C. A. La.). Obiter (ignorance held to excuse), In *re Stewart*, 24 A. B. R. 474, 178 Fed. 463 (D. C. N. Y.), quoted at § 639.

1. In *re Stewart*, 24 A. B. R. 474, 178 Fed. 463 (D. C. N. Y.), quoted at § 639.

2. Compare, ante, § 1307½. Also, *Atherton v. Green*, 24 A. B. R. 650, 179 Fed. 806 (C. C. A. Ills.), quoted ante, at § 1307½.

fore the bankruptcy of a stockbroker, and issued in the customer's name, obviously must be surrendered to the claimant.³

§ 1883. "Tracing Trust Funds."—If trust property or other property belonging to another in the control of the bankrupt and passing into the custody of the receiver or trustee, or the proceeds of such trust property, or the proceeds of property not belonging to the bankrupt but sold or conveyed away by him or by the receiver or trustee, can be traced into the receiver's or trustee's hands, they may be recovered from the receiver or trustee, provided the rights of innocent third parties are not prejudiced.⁴

Smith v. Township, 17 A. B. R. 749 (C. C. A. Mich.): "Where, as in this case, a wrongdoer knowingly mingles the property of another with his own in such manner that it becomes undistinguishable, the true owner may claim the whole mass, or if it has been disposed of, may follow it, or its proceeds as the case may be, as long as he can trace them, for the purpose of fastening an equitable lien for the property of which he has thus been dispossessed."

In re Acheson Co., 22 A. B. R. 338, 170 Fed. 427 (C. C. A. Ore.): "The doctrine of equity as sustained by the Supreme Court in *National Bank v. Insurance Co.*, 104 U. S. 65, 26 L. Ed. 693, approving the rule in *Hallett's Estate*, 13 Ch. Div. 696, 36 Moak's Eng. Rep. 779, is that if property is intrusted to another to sell and pay over the proceeds, and sale is made, the beneficial owner is entitled to the proceeds, whatever be their form, provided only he can identify them. If the proceeds cannot be identified because the trust money is mingled with the money of the trustee, then the cestui que trust is entitled to a charge upon the new investment to the extent of the trust money traceable into it. Justice Matthews writes of the rule as going far enough to cover not alone express trustees and agents, but bailees, rent collectors, or 'anybody else in a fiduciary position,' and as making 'no difference between investments in the purchase of lands or chattels or bonds or loans or moneys deposited in a bank account,' and he shows very clearly that the foundation of the doctrine rests upon the 'very idea of trusts,' which can only be preserved by a strict enforcement of the principle that one who holds a relationship of trust is not allowed to make private use of trust property."

In re Berry & Co., 16 A. B. R. 567; S. C., 17 A. B. R. 491, 148 Fed. 208 (C. C. A. N. Y.): "When the money was paid under a plain mistake of fact equity

3. *In re Meadows, Williams & Co.*, 24 A. B. R. 251, 177 Fed. 1004 (C. C. A. N. Y.), affirming 23 A. B. R. 124, 173 Fed. 694.

4. *In re Richards*, 4 A. B. R. 700, 104 Fed. 792 (D. C. Tenn., distinguished *In re Wood & Malone*, 9 A. B. R. 615, 121 Fed. 599); *In re Marsh*, 8 A. B. R. 576, 116 Fed. 396 (D. C. Conn.); *In re Colli*, 1 A. B. R. 625 (Ref. Mich.). See, *In re Howard*, 14 A. B. R. 296, 135 Fed. 721 (C. C. A. Calif.), where *Bills v. Schliep*, 11 A. B. R. 607, 127 Fed. 103 (C. C. A. N. Y.), again appears as res adjudicata.

Instances, *Erie R. R. Co. v. Dial*, 15 A. B. R. 559, 140 Fed. 689 (C. C. A. Ohio); *In re N. Car. Car Co.*, 11 A. B.

R. 490, 127 Fed. 178 (D. C. N. C.); *In re Graff*, 8 A. B. R. 744, 117 Fed. 343 (D. C. N. Y.); *In re Oliver*, 12 A. B. R. 694, 132 Fed. 588 (D. C. Tex.); *In re Ryttenberg v. Schaefer*, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.); *In re McCallum*, 7 A. B. R. 596, 113 Fed. 393 (D. C. Penn.); *In re City Bank*, 25 A. B. R. 276, 186 Fed. 250 (D. C. Mich.).

Instances, refused, *In re Smart*, 14 A. B. R. 672, 136 Fed. 974 (D. C. Ohio); *In re Taft*, 13 A. B. R. 417, 133 Fed. 511 (C. C. A. Ohio).

Impliedly, *In re Brown*, 22 A. B. R. 659, 171 Fed. 281 (D. C. N. Y.).

Compare, also, ante, § 1307½.

impressed upon it a constructive trust which followed it through the bank and into the hands of the trustees."

Hutchinson v. LeRoy, 8 A. B. R. 20, 113 Fed. 202 (C. C. A. Mass.): "Where the property of any person has been without his consent and sometimes even with his consent, converted into money, the money may be followed in equity so far as it is possible to remark it, provided the rights of innocent strangers are not prejudiced."

In *re Dunn & Co.*, 28 A. B. R. 127, 193 Fed. 212 (D. C. Ark.): "Leaving for the present out of consideration the effect of § 8 of the act of June 25, 1910 amending the Bankruptcy Act [§ 47a (2)] it cannot be disputed that trustees and receivers in bankruptcy, as well as all other receivers, take the assets of the bankrupt in the absence of fraud, subject to all equitable liens in favor of third parties to the extent that such assets have been augmented by the wrongful act of the Bankrupt." Further quoted at § 1884.

In *re Mulligan*, 9 A. B. R. 8, 116 Fed. 715 (D. C. Mass.): "Equity does not regard the form under which the cestui's property exists. Not only the actual trust property itself, but any property substituted for it, or into which it has been converted, may be recovered."

Welch v. Polley, 11 A. B. R. 215, 177 N. Y. 117: "The plaintiff must be permitted to follow, if she can, her trust moneys into the hands of the trustee in bankruptcy, he having no greater right against her than the bankrupt, her trustee, possessed had he remained solvent.

"The other creditors of the bankrupt have no claim upon any of the funds derived from plaintiff's trust which can be fully identified.

"To the extent that plaintiff is able to follow the trust funds into the purchase price of the real estate, or into the bankrupt's estate generally, she points out moneys that are no part of the estate held by the bankrupt's trustee for general distribution among the creditors, and is entitled to have them restored to the trust for her benefit which is to continue during her life."

In *re Gaskell*, 12 A. B. R. 251, 139 Fed. 235 (D. C. Wash.): "In accordance with the principles of equity, the courts of this country, in dealing with estates of insolvent debtors, protect trust funds for the benefit of the beneficiaries, when it is possible to trace such funds and segregate the same from the assets of the insolvent."

In *re Royea*, 16 A. B. R. 141, 143 Fed. 182 (D. C. Wash.): quoting *National Bank v. Insurance Co.*, 104 U. S. 54, as follows: "As long as trust property can be traced and followed, the property into which it has been converted remains subject to the trust; and, if a man mixes trust funds with his, the whole will be treated as trust property, except so far as he may be able to distinguish what is his. This doctrine applies in every case of a trust relation, and as well to moneys deposited in bank, and to the debt thereby created, as to every other description of property."

Obiter, In *re Wilkesbarre Furn. Mfg. Co.*, 12 A. B. R. 472, 130 Fed. 796 (D. C. Penn.): "It was undoubtedly a fraud on the creditors of Harrower Bros. for Frank B. Harrower to appropriate the money derived from the sale of the firm stock in order to make good his individual delinquencies as trustee; and upon proof of this, if the fund could be sufficiently identified and traced, an order might have been obtained restoring it to where it belonged. * * * The right that is sought to be enforced is the return of moneys wrongfully included in the fund previously distributed, which should therefore have been specifically claimed and traced."

In *re McGehee*, 21 A. B. R. 656, 166 Fed. 928 (D. C. Ga.): "The Troup Com-

pany and McGehee had the right to make any contract as between themselves they saw proper, so far as the matters in controversy here are concerned. There is nothing illegal or wrong about the agreement between them, and as to them it would seem that the Troup Company had the right to claim all notes, accounts, and proceeds of sale of fertilizers in the hands of McGehee as its property until the notes due the company for fertilizers were paid. Treated either as a reservation of title or as an equitable lien arising from a written agreement between the parties, it is certainly valid as between them. Of course, this claim of the Troup Company would be subject to any intervening liens or conveyances without notice, inasmuch as the agreement was never recorded. It would also be subject to the rights of parties who gave credit to McGehee on the strength of his supposed ownership of this property without notice of any kind. Where money had been received from the fertilizers, and had gone into the general funds of McGehee, of course, there would be no rights on the part of the Troup Company. How far the creditors may have obtained rights to which the Troup Company's claims of priority should be subordinated is not shown by this record."

Obiter, Block, Trustee v. Rice, Trustee, 21 A. B. R. 691, 167 Fed. 693 (D. C. Pa.): "It may be conceded that if Rice collected \$750.00 of trust funds belonging to the Fine bankruptcy estate and held it intact in a separate fund, or if it be shown that he received the money and deposited it in his own bank account and that at all times after the receipt of the trust fund and its deposit that the net balance of his bank account exceeded the amount of the trust fund, that upon application, the Fine bankruptcy estate, by an order of court, could have secured possession of the fund so held by Rice, and under these conditions it may be that as against Rice's creditors a voluntary payment of this trust fund by Rice to the Fine bankruptcy estate within four months of the time of filing a petition in bankruptcy against him would be a lawful payment, although Rice knew at the time he was insolvent, and that such a payment would not be held to be preferential under the act." Quoted further at § 1884.

But if the trust fund cannot be traced, it cannot be recovered.⁵

In *re Dorr*, 28 A. B. R. 505, 196 Fed. 292 (C. C. A. Calif.): "Money due from a bankrupt as trustee, and which cannot be distinguished from any other moneys in his possession or under his control, or which is due from him only because he has used trust funds for his own purposes, or otherwise misapplied them, cannot be considered as property held by the bankrupt in trust."

In *re McIntyre & Co.*, 26 A. B. R. 51, 185 Fed. 96 (C. C. A. N. Y.): "While the doctrine of following trust funds has been much extended in the modern decisions, there has never been a departure in the federal courts from the prin-

5. In *re Mulligan*, 9 A. B. R. 8, 116 Fed. 715 (D. C. Mass.); In *re Smith, Thorndyke & Brown Co.*, 20 A. B. R. 312, 159 Fed. 268 (D. C. Wis., affirmed in 22 A. B. R. 350, 170 Fed. 900), quoted at § 1884; impliedly, as to part, In *re McGehee*, 21 A. B. R. 656, 166 Fed. 928 (D. C. Ga.), quoted *supra*; *Block, Trustee v. Rice, Trustee*, 21 A. B. R. 691, 167 Fed. 693 (D. C. Pa.), quoted at § 1883 and at § 1884; In *re (Fred) Dorr*, 21 A. B. R. 752 (Ref. Calif.); In *re Acheson Co.*, 22 A. B. R. 338, 170 Fed. 427 (C. C. A. Ore.), quoted *post*, § 1884; In *re*

Smith, Thorndyke & Brown, 22 A. B. R. 350, 170 Fed. 900 (C. C. A. Wis., affirming 20 A. B. R. 312, 159 Fed. 268); In *re A. O. Brown*, 23 A. B. R. 423, 175 Fed. 769 (C. C. A. N. Y.); *obiter, Atherton v. Green*, 24 A. B. R. 650, 179 Fed. 806 (C. C. A. Ills.), quoted at § 1307½. Compare facts in case where a summary order was sought on third person who had commingled the bankrupt's assets with his own. In *re Jack-ier*, 24 A. B. R. 790, 179 Fed. 720 (D. C. Pa.).

ciple that there must be some identification of the property sought to be charged with the trust funds. But in the present case the proof fails to establish even the first step necessary to establish the petitioner's claim, viz., that the certified check embraced the trust funds. What proof there is would rather indicate that they were not included in it, and that the drawing and charging of such check was a special transaction, because the balance at the beginning and the end of the day when it was drawn and charged was the same. Moreover, we are unable to hold that the petitioner's failure in proof is helped out by any presumption of law. But if there was any inference that the check included trust funds, they certainly lost all possibility of identification when the check was collected and a certificate of deposit substituted in its place, and when the certificate of deposit was canceled and the amount thereof credited upon the note."

In *re Larkin & Metcalf*, 30 A. B. R. 903, 202 Fed. 572 (D. C. S. Dak.): "There is no recognized ground upon which equity can pursue this fund and impose upon it the character of a trust, except upon the theory that the money is still the property of the petitioners. If the petitioners herein are to be permitted to follow the fund received by the bankrupts or their agents upon the sale of this flour, and recover it, it is because the property belongs to the petitioners whether in the form in which they parted with its possession or in a substituted form. Under the earlier rule, petitioners would have been required to identify it as the very property which they had confided to another.

"The modern and more equitable doctrine permits the recovery of a trust fund from any one, not an innocent purchaser, and in any shape into which it may have been transmitted, provided he can establish the fact that it is his property or the proceeds of his property or that his property has gone into it and remains in a mass from which it cannot be distinguished.

"The earlier English doctrine was to the effect that the owner of property entrusted to another could follow and retake the same from the possession of the holder whether he was agent, bailee, or trustee, or from others who were in privity with him, so long as they were not bona fide purchasers for value, and this irrespective of whether such property remained in its original form or had been changed into some other form, so long as it could be ascertained to be the same property or the proceeds of the same property but that the right ceased when the means of ascertainment failed. It was further held that such means of ascertainment failed when the property was in the form of money, and had been mixed and confused in a general mass of money of the same description. The more recent doctrine, however, follows the rule announced in *Re Hallett's Estate* (*Knatchbull v. Hallett*), 13 Ch. Div. 696, which is to the effect that, if money held by one in a fiduciary character has been paid by him to his account at his banker's the person for whom he held the money can follow it and has a charge on the balance in the banker's hands, and that if the depositor has commingled it with his own funds in the bank, and has afterwards drawn out sums upon checks in the ordinary manner, he must be held to have drawn out his own money in preference to the trust money, and that, if he destroyed the trust fund by dissipating it altogether, there remains nothing to be the subject of the trust; that only so long as the trust property can be traced and followed into others into which it has been converted does it remain subject to the trust."

In *re Stewart*, 24 A. B. R. 474, 178 Fed. 463 (D. C. N. Y.): "True, because of the fraud Mitchell did not part with his title to the deposits; but, if we cannot follow and identify such deposits as being a part of the funds that came into the hands of the trustee, on what principle is he entitled to a lien on the

other moneys or property of the bankrupt? Is it the law that identification of deposits in a bank, either the identical money, or the money deposited commingled with other money of the bank (in cases where the deposit was not a trust fund in the hands of the depositor), is unnecessary, and that in such cases the law impresses whatever is found in the bank with a trust for the benefit of the defrauded depositor? If the law establishes that the moneys deposited by Mitchell were held by Stewart in trust for him from the time of the deposits, and that a recognition of such trust by Stewart was unnecessary, and then presumes that the moneys drawn out in regular course of business by depositors and by Stewart came from the other funds in the bank, leaving Mitchell's untouched, then, of course, the money of Mitchell and the whole of it is considered as in the bank and now in the hands of the trustee in bankruptcy. But it seems to me that this is further than the courts have gone."

And the trust fund must be clearly traced.⁶

Plow Co. v. McDavid, 14 A. B. R. 653, 137 Fed. 802 (C. C. A. Mo.): "The owner of a fund which has been misappropriated by one who held it in trust cannot follow it in the hands of the trustee unless he can trace the trust fund in kind or in specific property into which it has been converted, or, if the fund has been mingled with the trustee's other property, to establish a charge on the mass of such property for the amount of this fund. In other words, he can secure a preference out of the proceeds of the estate of the insolvent only where he can trace the trust property or fund, in its original or some substituted form, in the estate which comes into the hands of the trustee."

Erie R. R. v. Dial, 15 A. B. R. 559, 140 Fed. 689 (C. C. A. Ohio): "We recognize that the rule only permits the following of the converted property into assets which can be traced as proceeds, and that the lien does not attach to assets in which neither the thing nor its value can be found."

In re Acheson Co., 22 A. B. R. 338, 170 Fed. 427 (C. C. A. Ore.): "We do not mean to be understood as holding that equity will grant to a cestui que trust relief against any assets in the hands of a trustee, for it will not go farther than to give a lien when the facts are that there remain in the estate specific funds or property which have increased the assets of the estate, and which represent the proceeds of the specific property intrusted to the bankrupt. * * * Moreover, if there has been expenditure, and the funds are gone, and no specific property or money is found instead of the funds, it is inequitable that some other property found should be applied to pay one creditor in preference to another. So, funds that have been dissipated or that have been used to pay other creditors, or that have been spent to pay current business expenses, are not recoverable, because they are gone, and there is nothing remaining to be the subject of the trust."

In re Kearney, 21 A. B. R. 721, 167 Fed. 995 (D. C. Pa.): "Since, therefore, the money was not traced into a particular fund or deposit or earmarked in any other way, the inevitable inference is that the check of May 25th was drawn against the general funds of the bankrupt, and was intended to prefer the payee, * * * After the trustee had established a prima facie case of preference, it then became the duty of the claimant to prove that the loan was impressed with a trust, and that the money could be followed, either with precision, or at least into a mass from which it might be extracted with reasonable certainty."

In re Brunsing, Tolle & Postel, 22 A. B. R. 129, 169 Fed. 668 (D. C. Calif): "The deposit, constituting the trust fund, is not, by the findings of the referee,

6. *In re Leigh*, 31 A. B. R. 379, 208 Fed. 486 (D. C. Ill.); also cases in preceding and subsequent notes to this section.

sufficiently traced as part of the assets of the bankrupt estate. The rule applicable in cases like this is thus stated by Gilbert, J., in *Spokane County v. National Bank*, 68 Fed. 979, 16 C. C. A. 81: 'Both the settled principles of equity and the weight of authority sustain the view that the plaintiff's right to establish his trust and recover his fund must depend upon his ability to prove that his property is in its original or a substituted form in the hand of the defendant.' In other words, the depositor is not entitled to an equitable lien upon the entire mass of the estate of the bankrupt, but only upon that portion of it into which his deposit can be traced. In the well-considered case of *Cavin v. Gleason*, 105 N. Y. 257, 11 N. E. 506, the court said: 'It is clear, we think, that upon an accounting in bankruptcy or insolvency a trust creditor is not entitled to a preference over general creditors of the insolvent merely on the ground of the nature of his claim; that is, that he is a trust creditor, as distinguished from a general creditor. We know of no authority for such a contention. The equitable doctrine that as between creditors equality is equity admits, so far as we know, of no exception founded on the greater supposed sacredness of one debt, or that it arose out of a violation of duty, or that its loss involves greater apparent hardship in one case than another, unless it appears in addition that there is some specific recognized equity founded on some agreement, or the relation of the debt to the assigned property, which entitled the claimant, according to equitable principles, to the preferential payment.'" Quoted further at § 1884.

And the tracing of a trust fund cannot be converted into a proceedings to recover a preference—the two positions are antagonistic.⁷

Where a certified check was drawn on the trust fund and deposited with another bank which eventually cashed the certified check and substituted its own certificate of deposit, it was held that the tracing was unsuccessful so far as it sought to hold the other bank which had substituted its own certificate of deposit, but was successful as to the balance remaining in the first bank, in which the claimants were entitled to share pro rata.⁸

Also the fund must continue to exist: the doctrine of tracing trust funds will not permit the affixing of a trust upon property of a different species,⁹ unless such property be proved to be the direct product of the fund.

The burden of proof in the tracing is upon the claimant.¹⁰

But a deposition for proof of debt is not prima facie evidence.

In *re Jones*, 18 A. B. R. 208, 151 Fed. 108 (D. C. Mich.): "The referee rightly refused to allow priority upon the ground that the estate in the hands of the trustee in bankruptcy had been increased by the amount of the guardianship funds,

7. Impliedly, In *re Wilkesbarre Furn. Mfg. Co.*, 12 A. B. R. 472, 130 Fed. 796 (D. C. Penn.).

8. In *re McIntyre & Co.*, 26 A. B. R. 51, 185 Fed. 96 (C. C. A. N. Y.), quoted at § 1883.

9. In *re Stewart*, 24 A. B. R. 474, 178 Fed. 463 (D. C. N. Y.), quoted at § 1884.

10. In *re Marsh*, 8 A. B. R. 576, 116 Fed. 396 (D. C. Conn.); In *re Mulligan*, 9 A. B. R. 8, 116 Fed. 715 (D. C. Mass.); impliedly, In *re Jones*, 18 A. B.

R. 208 (D. C. Mich.). Compare, § 1884; *Block, trustee, v. Rice, trustee*, 21 A. B. R. 691, 167 Fed. 693 (D. C. Pa.), quoted supra; In *re Kearney*, 21 A. B. R. 721, 167 Fed. 995 (D. C. Pa.), quoted supra; In *re Acheson Co.*, 22 A. B. R. 338, 170 Fed. 427 (C. C. A. Ore.), quoted post, § 1884; In *re Stewart*, 24 A. B. R. 474, 178 Fed. 463 (D. C. N. Y.), quoted also at § 1884; In *re J. V. Lindsley & Co.*, 25 A. B. R. 239, 185 Fed. 684 (D. C. Mich.).

through the mingling of the same by the guardian with his own assets. Had the allegations referred to been proven the priority claimed might have been established. * * * But no proofs were introduced in support of the allegations mentioned. The certificate of the referee is express that 'No proof was submitted aside from proof of claim originally filed,' and that the 'claim was submitted upon such proof and argument of counsel.'

"It is contended by the petitioner that, as the petition was sworn to, the truth of the allegation in question is *prima facie* established upon the principle that the sworn proof of claim against the bankrupt is *prima facie* evidence of its allegations, even if objected to. This is undoubtedly the rule, as applied to the proof of the claim itself as a general claim, considered apart from the question of priority."

But compare, *obiter*, wherein the court seems to fail to note that the deposition is, at best, merely *prima facie* proof of "*debt*," not proof of "*conversion*," In *re McIntyre & Co.*, 24 A. B. R. 1, 176 Fed. 552 (C. C. A. N. Y.): "He contends, however, that the allegations of his proof of claim constituted *prima facie* evidence of conversion and that the burden was upon those objecting to his claim to show that the bankrupts at all times had their shares or their equivalent in their possession or under their control. Concededly this was not affirmatively shown, and, consequently, he urges that his claim must stand as established. It is undoubtedly true that a sworn proof of claim has probative force. It is *prima facie* evidence of its allegations even when objected to. There would, therefore, be much force in the claimant's contention if he had taken the same position before the referee. He might properly have stood upon his proof of claim and have insisted that the objections should go forward. But he did not do so. He offered to establish the allegations of his proof of claim by the entries in the stock record book and contended that the inference to be drawn therefrom supported the charge of conversion. Having thus attempted to establish the allegations in his proof of claim, he cannot be permitted to use those very allegations to supply the deficiencies in his testimony. A proof of claim may have some probative force but it certainly should not be regarded as self-proving unless relied upon."

The rule as to the tracing of trust funds is founded on equity and is not dependent on contract; and where a trust fund is mingled with the property of the trustee, the question whether the owner of the fund is entitled to a preference does not depend upon the construction of any contract between the parties, but upon a rule of preference in equity; and as to that the federal decisions must control and not those of the State where the contract was made.¹¹

11. *Plow Co. v. McDavid*, 14 A. B. R. 653, 137 Fed. 802 (C. C. A. Mo.); In *re Dorr*, 21 A. B. R. 752 (Ref. Calif.).

Instances of tracing alleged trust funds successfully and unsuccessfully:

(a) Proceeds of collaterals; In *re Marsh*, 8 A. B. R. 576, 116 Fed. 396 (D. C. Conn.).

(b) Conditional subscription to additional stock to pay off debts, the subscription being conditional on all paying in a like per cent. the money to be returned on failure to so pay in, some fail to pay in. Those paying in were entitled to recover in full. In *re N.*

Carolina Car Co., 11 A. B. R. 490, 127 Fed. 178 (D. C. N. Car.).

(c) Partner misappropriating firm assets to make good a shortage in his accounts as trustee in bankruptcy, *obiter*, In *re Wilkesbarre Furn. Mfg. Co.*, 12 A. B. R. 472, 130 Fed. 796 (D. C. Penn.).

(d) Factors' and principals' funds commingled, *Bills v. Schliep*, 11 A. B. R. 607, 127 Fed. 103 (C. C. A. N. Y.); *Ryttenberg v. Schaefer*, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.).

(e) Following proceeds of converted shares of stock, In *re Bolling*, 17 A. B.

In re Berry & Co., 16 A. B. R. 567 (S. C., 17 A. B. R. 491, 149 Fed. 208, C. C. A. N. Y.): "The rule invoked by the District Court is well stated by Judge Story: 'The receiving of money, which consistently with conscience cannot be retained, is in equity sufficient to raise a trust in favor of the party for whom, or on whose account, it was received. This is the governing principle

R. 399 (D. C. Va.); In re Graff, 8 A. B. R. 744, 117 Fed. 343 (D. C. N. Y.). Also similar stock bought, after conversion of customer's stock, presumed bought to replace converted shares, In re Brown & Co., 22 A. B. R. 659, 171 Fed. 281 (D. C. N. Y.).

(f) Consigned goods sold partly by bankrupt, partly by assignee before bankruptcy, In re McCallum, 7 A. B. R. 596, 113 Fed. 393 (D. C. Penn.).

(g) Consigned, or trust, goods sold and proceeds lost in stock speculation, In re Mulligan, 9 A. B. R. 8, 116 Fed. 715 (D. C. Mass.).

(h) Township treasurer depositing public moneys with private banker who becomes bankrupt, In re Smart, 14 A. B. R. 672, 136 Fed. 974 (D. C. Ohio). Compare, In re Salmon & Salmon, 16 A. B. R. 626 (D. C. Mo., on review sub nom. In re Blake, 17 A. B. R. 668).

(i) Township treasurer becoming bankrupt, having commingled public moneys with his private funds, Smith v. Township, 17 A. B. R. 475, 150 Fed. 257 (C. C. A. Mich.).

(j) Recovering public moneys deposited with bankrupt bank where collusive and fraudulent combination existed among banks, In re Salmon & Salmon, 16 A. B. R. 626, 143 Fed. 395 (D. C. Mo.).

(k) Draft drawn by landlord on agent for future rents and discounted at bank, held to be an equitable assignment of the rents when they later arise and to be good against the landlord's trustee in bankruptcy, In re Oliver, 12 A. B. R. 694, 132 Fed. 588 (D. C. Tex.).

(l) Money paid to bankrupt by mutual mistake. In re Collisi, 1 A. B. R. 625 (Ref. Mich.).

(m) Bank remitting to bankrupts the proceeds of a collection, in ignorance of the bankrupt's retention of the proceeds of a counter collection; no trust, In re Northrup, 20 A. B. R. 86, 159 Fed. 686 (C. C. A. N. Y.).

(n) Infant repudiating contract of employment may not have priority not allowed by § 64 (b) on the theory that he is asking for the proceeds of labor, title to which, by the repudiation, did not pass to the trustee, In re Hunttenberg, 18 A. B. R. 697, 153 Fed. 768 (D. C. N. Y.).

(o) Proceeds of note and stock held by bankrupts as trustees under a will

but "loaned" to themselves, Hatch v. Curtin, 19 A. B. R. 82, 154 Fed. 791 (C. C. A. Mass.).

(p) Notes, accounts and other proceeds of sale of goods, where the contract provided that the goods should remain the property of the seller until sold and that the proceeds of sale including notes, accounts, etc., should be kept separate as a trust fund to be turned over to the seller as collateral security, In re McGehee, 21 A. B. R. 656, 166 Fed. 928 (D. C. Ga.).

(q) Trustee in bankruptcy himself becoming bankrupt—funds of estate not successfully traced, Block, Trustee v. Rice, Trustee, 21 A. B. R. 691, 167 Fed. 693 (D. C. Pa.), quoted at §§ 1883, 1884.

(r) Money loaned to pay for license not traced, In re Kearney, 21 A. B. R. 721, 167 Fed. 995 (D. C. Pa.).

(s) Funds of a grocers' association deposited by its treasurer in the funds of a trading corporation of which he was also president and which became bankrupt, In re Smith, Thorndyke & Brown, 22 A. B. R. 350, 170 Fed. 900 (C. C. A. Wis.).

(t) Stock paid for by customer but still in hands of correspondent of stockbroker in another city, who is retaining it as security for unpaid balance between correspondent and bankrupt, bankrupt having failed to remit price, such correspondent also having lien on bankrupt's stock exchange seat, In re Meadows, Williams & Co., 23 A. B. R. 124, 173 Fed. 694 (D. C. N. Y.).

(u) In re Berry & Co., 16 A. B. R. 567; S. C., 17 A. B. R. 491, 148 Fed. 208 (C. C. A. N. Y.).

(v) Money collected for third party on eve of bankruptcy of the collector, Smith v. Mottley, 17 A. B. R. 864 (C. C. A. Ohio).

(w) Sale of merchandise in bulk under statutes requiring notices to creditors, etc., where the purchaser goes into bankruptcy, the seller having complied with the law as to the giving of notice: the merchandise and its proceeds (less proportionate expenses) constitute a trust fund for the creditors of the seller, In re Gaskill, 12 A. B. R. 251, 130 Fed. 235 (D. C. Wash.).

(x) Proceeds of property sold as del credere agent, kept separate from general estate but commingled with pro-

in all such cases. And, therefore, whenever any interest arises the true question is, not whether money has been received by a party, of which he could not have compelled the payment, but whether he can now, with a safe conscience, *ex æquo et bono*, retain it. Illustrations of this doctrine are familiar in cases of money paid by accident or mistake or fraud. * * * Still, however, there are many cases of this sort, where it is indispensable to resort to courts of equity for adequate relief, and especially where the transactions are complicated, and a discovery from the defendants is requisite.’”

And the rules are not altered by the bankruptcy of the holder of the fund, for neither by the bankrupt’s “transfer by any means” nor by any levy “under judicial process” could the *cestui que trust* be deprived of the right, and it is only as to property that could be so transferred or levied on that title passes to the trustee.

In *re Royea*, 16 A. B. R. 143 (D. C. Wash.): “Section 70 (a) prescribes the rule to be applied in the determination of questions as to what property vests in the trustee of a bankrupt’s estate. The rule of the statute is that the trustee shall be vested by operation of law with the title of the bankrupt as of the date he was adjudged a bankrupt, to property, not exempt, which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him.

“Consideration of this rule leads to the inquiry whether the bankrupt, after he had become insolvent and immediately before the petition was filed, could have transferred the balance to his credit in the bank, so as to have defeated the petitioner in a suit in equity to reclaim his part of it, or whether an attaching or execution creditor, by levying upon the balance in the bank under judicial process against the bankrupt, could have divested the petitioner of his beneficial interest in the fund? To this inquiry equity gives a negative answer.”

And the rule does not differ, where the trust funds have been rightfully acquired, from what it is where they have been wrongfully acquired.

Smith v. Mottley, 17 A. B. R. 866, 150 Fed. 266 (C. C. A. Ohio): “But it makes no difference in the application of the principle of that decision that in one instance the wrongdoer was lawfully in the possession of the property and in the other not. The critical fact is in the wrongful appropriation by one party of the property of another by mingling it indistinguishably with his own, and it is not ordinarily important by what means he became possessed of the property.”

But a trust must exist, else tracing will not avail.¹²

In *re Northrup*, 20 A. B. R. 86, 159 Fed. 686 (C. C. A. N. Y.): “The conversation was wholly inadequate to vest in the Syracuse Bank any title—

ceeds of similar sales. In *re Taft*, 13 A. B. R. 417, 133 Fed. 511, 66 C. C. A. 385.

(y) Conversion of goods taken from carrier by buyer before payment where sold C. O. D. *Erie R. R. v. Dial*, 15 A. B. R. 559, 140 Fed. 689 (C. C. A. Ohio).

(z) Agreement to give contempora-

neous mortgage to secure purchase price, disregarded and goods commingled, seller has lien on whole. In *re Hennis*, 17 A. B. R. 889 (Ref. N. Car.).

12. No tracing of money paid, where annuity purchased in fraud of creditors set aside. *Smith v. Mut. Life Ins. Co.*, 24 A. B. R. 514, 178 Fed. 510 (C. C. Mass.).

equitable or other—in the collections which it remitted for, or to operate as a substitution of funds. It did not constitute a declaration of trust.”

And in the absence of an express trust there must be some breach of good faith, or some fraud or unconscientious conduct to give rise to the equity.

In *re Smith, Thorndyke & Brown*, 20 A. B. R. 312, 159 Fed. 268 (D. C. Wis.): “It is sometimes profitable to lay aside elaborate briefs, burdened with a multitude of citations, and refer to an elementary principle, which is, after all, the pivot upon which the case must turn. Much has been said in the argument about trusts and trustees, trust moneys, etc. As applied to this case the word ‘trust’ is little more than a figure of speech. It is called by the law writers a constructive trust. Mr. Pomeroy, in his work on *Equitable Jurisprudence* (section 1044), uses the term ‘trust in invitum,’ and the learned author well describes how and why the court of equity has resorted to this fiction to facilitate its peculiar jurisdiction and to work out justice in peculiar cases. It is elementary that, in every instance where the court creates this quasi trust relation, it must find either actual fraud or some unconscientious conduct. In such case the court will fasten upon the property in the hands of the offending party and will convert him into a trustee of the legal title. It may be nothing more than a breach of good faith, as a mingling by an agent of the funds of his principle with his own moneys, or the receipt of a deposit by the officers of a bank when they know the bank to be hopelessly insolvent. There are innumerable variations of tortious conduct which will warrant this interposition of a court of equity; but in every such case there must be at the bottom some unfair dealing or wrongdoing. In the instant case the evidence shows without contradiction that Smith, as treasurer of the Grocers’ Association, was at liberty to deposit its funds with the Smith, Thorndyke & Brown Company, that such company were to use such funds, and that disbursements therefrom were to be made by checks upon such company; in other words, nothing has been done either by Smith, or the Smith, Thorndyke & Brown Company, which was not contemplated by the parties, and therefore there would appear to be no just occasion for the application of the trust doctrine.”

And a mere general deposit, giving rise to the relation of debtor and creditor rather than to that of bailee and bailor, or trustee and cestui qui trust, will not constitute a “trust fund.”¹³

But the doctrine is well established that the receiving of deposits by a bank on the eve of insolvency with knowledge of such insolvent condition, does not give rise to the relation of debtor and creditor but produces a trust fund reclaimable by the depositor.

In *re Silver*, 31 A. B. R. 106, 208 Fed. 797 (D. C. Ohio): “We hold then that the facts surrounding this transaction justified petitioners’ claim that the bankrupt legally knew of the insolvency of his business when he received the deposits in question. The implied contract, therefore, which ordinarily arises to create the relation of debtor and creditor when deposits are made in a banking institution

¹³ But a bank receiving deposits holds itself out thereby as solvent, and is guilty of fraud if it knows that it is insolvent; *St. Louis & San Francisco Ry. Co. v. Johnston*, 133 U. S. 566, 576.

never was created, and a trust impressed upon these funds in behalf of these several depositors is the equitable result of these transactions."

In *re Smith, Thorndyke & Brown*, 20 A. B. R. 312, 159 Fed. 268 (D. C. Wis.): "The Grocers' Association had practically consented to employ Smith, Thorndyke & Brown as a bank. * * * There is in the present case no semblance of bailment, because the deposit was general, not special. All that was required of Smith, Thorndyke & Brown Company was to return on demand an equivalent sum. Can there be any doubt, therefore, that as between these original parties there subsisted the relation of debtor and creditor? And, if so, Mrs. Smith by virtue of her assignment became a creditor, and must share *pari passu* with other creditors under the terms of the Bankruptcy Act."

In *re Nichols*, 22 A. B. R. 216, 166 Fed. 603 (D. C. N. Y.): "Wheeler drew his checks against this from time to time, and it appears from the book that at times he made an overdraft, and that at other times there was a large amount to his credit. There was no agreement that Nichols should hold and keep these moneys separate and distinct from his other funds, or that he should not use them in the usual course of his banking business. The relation of the parties was that of debtor and creditor. Nichols, of course, knew that he was receiving the funds of the town, as he knew that Wheeler was the supervisor thereof, and that the funds deposited by Wheeler as supervisor were held by him in that capacity, and for the town and the school districts, etc. This, however, gave Wheeler no lien of claim upon the funds or moneys of Nichols. So far as capable of identification Wheeler could have held the funds as against the other creditors of the bankrupt, but no further."

The Amendment of 1910 to § 47a (2), endowing the trustee with the rights of a creditor "armed with process," does not, in general, affect the right to trace trust funds.

In *re Dunn & Co.*, 28 A. B. R. 127, 193 Fed. 212 (D. C. Ark.): "The next question to be determined is: What is the effect of the amendatory act of 1910? * * * The trustee, therefore, is entitled to the same rights an execution creditor would have if the money in controversy had been seized by an officer under writ of attachment of execution, or if deposited in the bank, a writ of garnishment had been served on the depository. Would such proceedings defeat the claim of intervener? * * *

"An attaching or execution creditor is not a bona fide purchaser entitled to the protection the law affords such purchasers. He can only acquire by the seizure such titles or interest as the execution defendant has. The rule that, as money has no earmarks, every one is to be treated as an innocent purchaser, has been modified in cases of this nature."

§ 1884. Commingling of Trust Funds or Trust Property.—If the proceeds of the trust fund are deposited in bank to the bankrupt's general account, or otherwise commingled with the bankrupt's own funds, the amount may be ordered paid over in full, notwithstanding the commingling, for the trust funds will have priority over those not trust funds.¹⁴

14. In *re Berry & Co.*, 16 A. B. R. 564, 146 Fed. 623 (S. C., 17 A. B. R. 591, C. C. A. N. Y.).

Hutchinson v. LeRoy, 8 A. B. R. 20 (C. C. A. Mass.): In this case a pledgee of stock re-pledged the stock to

a bank to secure his own debt and thereafter became bankrupt: the court held the pledgor might recover from the trustee the proceeds of the sale of the stock if he could trace them into the trustee's hands, less the re-pledgee's

In *re Dunn & Co.*, 28 A. B. R. 127, 193 Fed. 212 (D. C. Ark.): "Nor could there be any doubt that trust funds which have been fraudulently diverted or appropriated can be recovered of a receiver whenever such funds are susceptible of identification in the hands of the possessor, or, if they have been intermingled with the general funds of the trustee so as to render their identification impossible, a court of equity (and bankruptcy courts are courts of equity in proceedings of this nature) will follow them and decree restitution to the *cestui que trust* if the unlawful appropriation of the trust fund resulted in swelling or increasing the assets of the insolvent and came to the possession of the trustee." This case quoted further post, this section, and ante, § 1883.

In *re Woods and Malone*, 9 A. B. R. 615, 121 Fed. 599 (D. C. Ga.): "The doctrine of Lord Ellenborough that this principle does not apply, when the subject is turned into money and confounded in a general mass of the same description, is repudiated, for said the learned Master of the Rolls: 'Equity will follow the money even if put into a bag or undistinguishable mass, by taking out the same quantity. And the doctrine that money has no earmark must be taken as subject to the application of this rule.'"

In *re Mulligan*, 9 A. B. R. 8, 116 Fed. 715 (D. C. Mass.): "Still again, if the trust fund has been mingled with funds which belong to the defaulting trustee, and the mingled mass has been converted into property which exists in specie, the *cestui* has a claim upon this property by way of lien for the replacement of the trust fund advanced for the purchase, or by way of equitable ownership of an aliquot part of the property, either or both. For the purposes of this discussion, it matters not which. This principle is apparently questioned in *Litchfield v. Ballou*, 114 U. S. 190, 195; but the doubt must be limited to the particular case, as the principle has been abundantly recognized. The recognition has been most complete where the trustee has mingled in one bank deposit the trust fund and moneys of his own. Whatever may have been his actual intention, he will be presumed to have acted honestly, so far as the state of the account allows the presumption. His drafts against the deposit thus mingled are taken to be applied to his own share of the deposit until that share is exhausted, and what is left is taken to belong in equity to the *cestui que trust*. The rule thus stated is not undisputed (see *Steamboat Co. v. Locke*, 73 Me. 370), but it is supported by the weight of authority. *Bank v. Peters*, 123 N. Y. 272, 25 N. E. 319; *Mercantile Trust Co. v. St. Louis & S. F. R. Co.* (C. C.), 99 Fed. 485; *Bank v. Roller*, 85 Md. 495, 37 Atl. 30, 36 L. R. A. 767,

claim and the original debt due the bankrupt, where at all times the trustee had enough in his hands to cover such amount.

Smith v. Mottley, 17 A. B. R. 863, 150 Fed. 266 (C. C. A. Ohio). Compare, In *re Swift*, Ex parte LeRoy, 5 A. B. R. 232 (Ref. Mass.); inferentially, In *re Graff*, 8 A. B. R. 744 (D. C. N. Y.).

In *re McGehee*, 21 A. B. R. 656, 166 Fed. 928 (D. C. Ga.), quoted at § 1883, is not contra, for there, doubtless, the "general fund" mentioned did not refer to an existent actual fund or deposit, but probably referred to the fact that the proceeds had already been spent for general purposes. See, obiter, In *re A. O. Brown*, 23 A. B. R. 423, 175 Fed. 769 (C. C. A. N. Y.).

In *re Stewart*, 24 A. B. R. 474, 178 Fed. 463 (D. C. N. Y.), quoted in this same section; instance, In *re City Bank*, 25 A. B. R. 276, 186 Fed. 250 (D. C. Mich.).

[England] *Knatchbull v. Hallett*, 13 Ch. Div. 696, 36 Eng. Rep. 779: "If a person who holds money as a trustee, or in a fiduciary character, pays it to his account at his bankers and mixes it with his money, and afterwards draws out sums by check in the ordinary manner. Held, that the rules * * * attributing the first drawings out to the first payments in, does not apply, and that the drawer must be taken to have drawn out his own money in preference to the trust money."

60 Am. St. Rep. 344; *In re Hallett's Estate*, 13 Ch. Div. 696, 36 Eng. Rep. 779; *McMahon v. Fetherstonhaugh* (1895); 1 Ir. R. 83. In some cases, indeed, this rule concerning bank deposits has been extended to cases in which the bank itself is the defaulting trustee. The cestui has sometimes been allowed a charge prior to that of the general creditors upon the general cash assets of the defaulting bank, or upon the minimum value of these cash assets since the date of the trust deposit. If since that date the cash assets have at any time fallen below the amount of the trust deposit, it has been held that the trust fund has been finally dissipated to that extent. *Merchants' Bank v. School Dist.*, 36 C. C. A. 432, 94 Fed. 705; *Commissioners v. Wilkinson*, 119 Mich. 655; *Bank v. Weens*, 69 Tex. 489. See *Bank v. Down* (C. C.), 38 Fed. 172; *Appeal of Carmany*, 166 Pa. 622."

To same effect, *Erie R. R. v. Dial*, 15 A. B. R. 559, 140 Fed. 689 (C. C. A. Ohio): "Knowing that these goods could not be lawfully taken until they were paid for, and that the railroad company had no authority to deliver them without payment, the rubber company seized an opportunity for wrongfully obtaining possession of the goods and proceeded to commingle them with its own. The title of the shippers was not divested by this trespass. It did not convert the railroad company into a debtor to the shippers, whatever the liability of the railroad company for negligence might be, or the rubber company into a debtor of the railroad company.

"The trustees say that the rubber company converted the rubber into tires and commingled them with other tires which it had on hand, and that the property can be no longer identified. But the vendors of the rubber never consented to this. In a common-law court this might, as between the owners and the trespasser, have given title to the owners of the whole mass of tires, if they were indistinguishable. But a court of equity, for the purpose of saving to creditors that value which attached to the things before owned by the trespasser, will forbear to enforce a confiscation, and, instead, will accord a lien to the owner upon the mass for the value of the things converted. We had occasion to consider this subject in *Holder v. Western German Bank*, 136 Fed. 90, 68 C. C. A. 554, where we held, upon the authority of *Knatchbull v. Hallett*, 13 Ch. Div. 696, 36 Eng. Rep. 779, and *National Bank v. Insurance Co.*, 104 U. S. 54, that, where the tort-feasor had mingled the property of the owner with his own, a lien would attach to the mass pro tanto. The assets came to the trustee in this condition. His interest therein is no other nor greater than that of the bankrupt, except where the bankrupt has conveyed his property with intent to defraud his creditors."

Smith v. Township, 17 A. B. R. 749, 150 Fed. 257 (C. C. A. Mich.): "When the commingled property is of more value than that wrongfully taken, it is equitable that the excess should go to the creditors of the wrongdoer, although by the strict rule of the common law the whole mass might become the property of the innocent owner of the portion misappropriated. Justice requires that the rights of innocent third parties having acquired the property, or some interest in it, for value, should be protected, and against such the rule is not enforced. But here the trustee stands in the shoes of the bankrupt and has only his rights. Of course, we are speaking of the general rule, and do not need to notice the instances of conveyances and preferences fraudulent as against creditors. And the question is what were the respective rights of the township and the bankrupt when the creditors filed their petition against him. The bankrupt's trustee says that it is impossible to find out what parts of the stock of goods contain the money of the township, and this was the difficulty which the referee found and which controlled his decision. But it was not for the

township to make the distinction. As said by Chancellor Kent in *Hart v. Ten Eyck*, 2 Johns Ch. 62, at page 108, 'If a party having charge of the property of others, so confounds it with his own, that the line of distinction cannot be traced, all the inconveniences of the confusion is thrown upon the party who produces it, and it is for him to distinguish his own property, or lose it.' That case presented a state of facts which in this respect was quite similar to those which existed here. The fair inference is that the bankrupt took the money from time to time, purchased goods and mingled them with his stock, and out of his stock he sold parcels, which were not distinguishable in respect of the means with which they were bought. From the beginning of his fraudulent intermixture of his own money and that of the township, or of goods which may have been bought with his own money and others bought with the money of the township, if the latter did not become the owner of the commingled stock, it had, at least, a lien upon it for reimbursement; and the continuance of such transactions operated in the same way."

In *re Royea*, 16 A. B. R. 142, 143 Fed. 182 (D. C. Wash.): "The main argument in opposition to the petition is that trust money must be earmarked or separately kept in order to entitle the cestui que trust to reclaim it, in opposition to creditors of an insolvent debtor, and that where a bankrupt has mingled trust funds with his own, so that the identity of the trust company is lost, the beneficiaries of the trust must share *pari passu* with the creditors. * * *

"In many of the reported cases the cestui que trust failed to prove that the fund or property sought to be impressed with the trust, in fact, included trust money or acquisitions by reinvestment or exchange of trust money or property, and on that ground adverse decisions were rendered, without combating the doctrine of the Supreme Court, as expounded in the opinions by Mr. Justice Matthews above cited. In this case, although the money cannot be specifically identified, the fund is clearly proved to have been enlarged by mingling trust money with other money, and the equitable right of the petitioner to reclaim an amount equivalent to the amount intrusted is clear."

Block, trustee, v. Rice, trustee, 21 A. B. R. 691, 167 Fed. 693 (D. C. Pa.): "But the difficulty the defendant encounters in setting up that defense here is that his right to follow this trust fund in the possession of Rice depends upon it having been kept separate, or upon its having been received by him, deposited in bank, and the net balance of his bank account at all times exceeding the \$750.00, and this must be made to appear by him to the satisfaction of the jury. The burden of showing this rests upon him. I recall no evidence whatever in the case to this effect." Quoted further ante, § 1883.

In *re Brunsing, Tolle & Postel*, 22 A. B. R. 129, 169 Fed. 668 (D. C. Calif.): "Of course, under this rule, it was not incumbent on the depositor, in the present case, to show that the identical merchandise purchased with his money passed into the hands of the trustee. If such merchandise was commingled with the bankrupt's general stock, and this general stock or the proceeds arising from the sale thereof, whether money, credits, or other property, can be shown to form a part of the assets of the bankrupt estate, the depositor would be entitled to an equitable preference in the distribution of such estate. In the case of *Cavin v. Gleason*, 105 N. Y. 256, 11 N. E. 504, above cited, the court, after stating that it is the general rule, as well in a court of equity as in a court of law, that in order to follow trust funds and subject them to the operation of the trust they must be identified, proceeded to say: 'A court of equity, in pursuing the inquiry and in administering relief, is less hampered by technical difficulties than a court of law, and it may be sufficient, to entitle a party to equitable preference in the distribution of a fund in insolvency, that it ap-

pears that the fund or property of the insolvent remaining for distribution includes the proceeds of the trust estate, although it may be impossible to point out the precise thing in which the trust fund has been invested, or the precise time when the conversion took place. The authorities require at least this degree of distinctness in the proof before preference can be awarded." Quoted further at § 1883.

Compare, *Bills v. Schliep*, 11 A. B. R. 607, 127 Fed. 103 (C. C. A. N. Y.): "It is immaterial that Turle & Skidmore may have mingled the funds in their hands received from the various shipments, because after such shipments and notice the law will presume and a court of equity would require either that Turle & Skidmore should satisfy their claims out of the other car loads in their hands before resorting to the car loads in question, or would be deemed to have held all proceeds not necessary to satisfy their claims for the use of the owners and consignors of the cargoes in question."

At any rate, such will be the case where at no time an adverse balance occurs.¹⁵

In *re Berry & Co.*, 16 A. B. R. 567, 146 Fed. 623 (C. C. A. N. Y., S. C., 17 A. B. R. 591): "The account of Berry & Co. was never overdrawn during the day of November 25; there was as much as \$5,000 to their credit during that day and at no time did the withdrawals reduce the balance below \$1,500. It is true that large sums were checked out after the deposit of the \$1,500, but the law presumes that the amounts withdrawn were not those impressed with the trust. In other words, so long as \$1,500 remained in the bank the presumption is that it was the trust fund."

But an adverse balance or an entire drawing out of all funds occurring at any time will destroy the tracing of the fund.¹⁶

In *re Mulligan*, 9 A. B. R. 8, 116 Fed. 715 (D. C. Mass.): "This is not the case of a bank account, which, as has been said, is affected by a rather artificial rule. Moreover, there is no proof that the requirements of that artificial rule have here been met. At some time after the check was handed to Hornblower, the balance of the account may have been against the bankrupt, and an adverse balance at any time after the trust deposit is made destroys the claim of the cestui upon a bank account in which trust funds and private funds have been mingled. That the funds were mingled, not by the bankrupt himself, but by his broker, does not give Brown Bros. a better claim."

In *re Smith, Thorndyke & Brown*, 20 A. B. R. 312, 159 Fed. 268 (D. C. Wis., affirmed in *re Smith, Thorndyke & Brown Co.*, 22 A. B. R. 350, 170 Fed. 900, C. C. A.): "There is another principle which would be equally fatal to the contention of the claimant. It appears that in February, 1907, the Smith, Thorndyke & Brown Company, being temporarily embarrassed, but supposed on all hands to be solvent, called in an attorney to look over its books, who found this account with Smith as treasurer appearing only upon the cash book, and showing a debit balance against the Smith, Thorndyke & Brown Company of about \$4,000, which had not been paid because the company had not

15. In *re A. O. Brown*, 23 A. B. R. 423, 175 Fed. 769 (C. C. A. N. Y.).

16. In *re Smith, Thorndyke & Brown*, 22 A. B. R. 350, 170 Fed. 900 (C. C. A. Wis.); In *re Dunn & Co.*, 28 A. B. R. 127, 193 Fed. 212 (D. C. Ark.), quoted

at §§ 1883 and 1884. Compare, inferentially and suggestively, but at best obiter, In *re Stewart*, 24 A. B. R. 474, 178 Fed. 463 (D. C. N. Y.), quoted in this same section.

funds available to pay the same. The attorney advised that this account should be transferred to the general ledger of the company, and that Smith should at once open an account with the bank as treasurer of the Grocers' Association, and thereafter deposit all funds of the association with the bank, which course was pursued. Between that time and June 10, 1907, the date of filing of the petition in bankruptcy, this balance of \$4,000 was reduced to \$2,156. Not a dollar of the association money came to the Smith, Thorndyke & Brown Company after February, 1907. The general bank balance of Smith, Thorndyke & Brown Company was appropriated by the bank under a banker's lien, which proceeding was sanctioned by the court, and no part of such money came to the hands of the trustee. Thus it appears that no part of the sum claimed ever found its way into the assets of the estate. It had been spent and dissipated four months before the bankruptcy proceedings. Under such circumstances no equitable doctrine could be invoked to appropriate general assets of the estate belonging to general creditors to make good this antecedent deficit; no portion of the fund having been traced into the estate."

So, also, the expenditure or dissipation of the trust fund will render the tracing of it ineffective.¹⁷ Thus, where the deposit was not special, but general. But where the trust funds are commingled, not only with private funds, but with other trust funds; and, after checking out, there remains at any time less than the trust fund in controversy, the claimants have failed *pro tanto* in tracing out their fund.¹⁸

In *re Dunn & Co.*, 28 A. B. R. 127, 193 Fed. 212 (D. C. Ark.): "On the other hand, if, at any time after misappropriation of the funds and mingling them with those of the wrongdoer, all the money is withdrawn, including that unlawfully mingled, the equities are lost, although moneys from other sources are subsequently placed in the same place. Or if a part of the funds so mingled is withdrawn and the fund reduced to a smaller sum than the trust fund, the latter must be regarded as dissipated except as to this balance. Sums subsequently added to the fund from other sources cannot be subjected to the equitable claim of the *cestui que trust*."

In *re T. A. McIntyre & Co.*, 25 A. B. R. 93, 181 Fed. 960 (C. C. A. N. Y.): "Bankrupts bought 200 shares of a certain stock for a customer. They did not keep this stock, but used it as they would their own in the general transaction of their business. They did the same with other customers who had bought like stock. When they failed there were 95 shares of this kind of stock among the Bank of Commerce collateral, 10 shares were pledged on another loan, and there were 2 shares in their vault. They owed their customers 1,651 shares of this variety of stock. We cannot find from the record any satisfactory identification of the 95 shares (or any of them) as being those bought for this particular customer, rather than those bought for some one else. He is not in the position of Pipey (see opinion filed today in *Re McIntyre* (C. C. A., 2d Cir.), 24 Am. B. R. 626, 181 Fed. 955), and is not entitled to the certificates."

Where there remains only enough to cover a part of the commingled fund, it would seem that the claimants should share *pro rata*¹⁹ since their

17. In *re J. V. Lindsey & Co.*, 25 A. B. R. 239, 185 Fed. 684 (D. C. Mich.).

18. In *re Mulligan*, 9 A. B. R. 8, 116 Fed. 715 (D. C. Mass.); inferentially,

Clafin Dry Goods Co. v. Eason, 2 A. B. R. 263 (Ref. Tex.).

19. In *re McIntyre & Co.*, 25 A. B. R. 93, 181 Fed. 960 (C. C. A. N. Y.).

losses date from the checking out. In the event, however, that some of the trust funds were deposited *after* some of the checking out of the already insufficient fund had occurred, it might become necessary to classify the claimants.

But the doctrine of the persistence of the trust fund over the commingled individual funds of the insolvent does not permit the affixing of the trust to property of a different species nor to the general assets;²⁰ unless, of course, such property of a different species be proved to be the direct product of the fund.

It has apparently been held, though the reasoning is not entirely clear, that the trust will not attach where subsequent withdrawals exceed subsequent additions to the fund to such an extent as to more than equal the trust fund.

Impliedly, *In re Stewart*, 24 A. B. R. 474, 178 Fed. 463 (D. C. N. Y.): "I had supposed that the burden was on the claimant to prove his case and show by a fair preponderance of evidence that his money was commingled in the common mass of money on hand. If the evidence shows, as here, that in all probability the money has been paid out to other depositors, prior depositors, and that the money remaining is that put in the bank by subsequent depositors, how can it be said that the funds are traced and found commingled with other funds? To so hold is to impress all subsequent deposits with the trust relation and obligation created by law when Stewart obtained Mitchell's money by the fraudulent concealment, and hold that there has been a mere change of funds inasmuch as all subsequent deposits became the property of Stewart, and that it is immaterial that no substantial part of Mitchell's original deposits remained when the bank closed. The result of such a holding is to give a depositor of six months or a year ago, who was ignorant of the hopeless insolvency of a bank known to the bank, or to the banker in case of a private bank, a lien on the moneys subsequently deposited by others and remaining in the bank at the time of failure, regardless of whether or not any of the money of such old depositor remains. If showing the deposit obtained by fraudulent concealment and the mingling of the funds with other deposits, and that there was always a balance greater than such deposits, although thousands of dollars were being deposited daily and other thousands drawn out, makes a case and throws the burden of proof on the trustee in bankruptcy to show that the moneys so deposited by the one asserting the fraud had been drawn out, it will be impossible to defend in the great majority of cases. While it is easy to show the money in, and that all deposits go into, a common mass from which payments are constantly being made in due course of business, it is impossible, with rare exceptions, to show what money was paid out. * * *

"I think the opinion in this case shows the holding to be that, where a bank collects paper intrusted to it for collection and misappropriates the money collected or fails to account for and pay same over, it is sufficient to show, in order to justify collection from the funds in the hands of the receiver when appointed, that the money so collected went into and were commingled with the moneys of the bank; that the balance of money on hand was thereafter never less than the amount so collected and misapplied even in cases

²⁰. *In re Stewart*, 24 A. B. R. 474, 178 Fed. 463 (D. C. N. Y.), quoted in this same section, *post*.

where there were large deposits and withdrawals by others; and that the balance of the moneys so commingled went into the hands of the receiver; but that it is not sufficient to show that the 'assets' of the bank were at all times greater than the amount misappropriated; and that such 'assets' came to the hands of the receiver. In short, the trust attaches to and follows the commingled fund so long as any of it remains, but never attaches to the general assets, or to funds deposited after the commingled fund has been drawn out. But if the commingled fund is being constantly augmented by new deposits and drawn upon, and the fund is not reduced below the deposits in question, then it is assumed as matter of law that identity is established."

But such holding, if it be the holding, does not seem entirely safe to follow in all cases. The further doctrine must not be lost sight of that such subsequent deposits or accretions as are not also trust funds become the individual property of the insolvent and will be presumed to have been used to *replace* the trust fund.

In accordance with the doctrine of the persistence of the trust fund, disbursements made by a bank with which a trust fund has been deposited, will be presumed to have been made from its own funds, and not from those of the trust account, unless the contrary has been established.²²

It has been held that where shares of stock belonging to a customer have been converted by a broker, other similar shares, subsequently purchased, will be presumed to have been bought to replace them, unless there were other customers of similar stock, in which event all would be entitled thereto as tenants in common.

In *re Brown*, 22 A. B. R. 659, 171 Fed. 281 (D. C. N. Y.): "The question is whether we should not assume that the broker, in taking from other funds enough to buy an equal number of shares of stock, did not intend pro tanto to attribute that much of his own funds to making good his default. By way of analogy, suppose that an agent depletes a bank deposit made in his name as agent. Subsequent deposits in that fund would go to make good the former conversion, and the general creditors could not complain. * * * He may make good his default out of his own property, and all that is necessary is some unequivocal appropriation of the property of that effect. Of course, in that case the appropriation was unambiguous, and here we must adopt a presumption; but the question is whether such a presumption is not usually borne out in fact. I think it is. I believe that brokers do usually mean their stocks on hand in the first instance to belong to their customers until they have enough to answer their obligations. If the bankrupts in this case in fact had no such intention, the receiver must show it. A manifest intention being enough, however, I shall adopt the presumption that the purchase of similar stock to that converted is the manifestation of such an intention. A more difficult question of fact arises in case the stock on hand turns out not to be enough to meet all the obligations to customers. Still in that case I think I must likewise assume in the absence of contradictory evidence, that the broker's intention was to contribute so much of the assets as he invested in this stock in general toward the fulfillment of such obligations. Each share being of equal value and unidentified, he cannot be said to have favored one customer rather

²². In *re City Bank*, 25 A. B. R. 276, 186 Fed. 250 (D. C. Mich.).

than another; nor can I say that, because all the obligations are not fulfilled by the stock which is left, therefore I must assume that he had no intention whatever of fulfilling any part of them. Of course, he did not complete his intention; but so far as he went I think I must assume that he intended to replace the stock which he should have, but did not have, on hand. To adopt the analogy suggested by Mr. Justice Holmes in his opinion in *Richardson v. Shaw*, supra, suppose an elevator man has depleted the elevator below the amount due to all depositors; when he subsequently puts back into the elevator enough, or part of enough, wheat to answer his obligations to all, the claimants become co-owners of it. Could the elevator man's general creditors claim that they were entitled to the subsequent accretions? Or suppose it could be shown that he had entirely emptied the grain elevator; is there any doubt that his subsequent filling of it, or partial filling of it, must be assumed to be an appropriation by him of so much of his property to make good his conversion? The analogy in law seems to me to be complete in spite of the diversity of the subject matter."

The burden of proof that the property has been wrongfully mingled in a mass of the property of the wrongdoer is upon the owner, but when this is shown, the burden shifts to the wrongdoer. It is for him to distinguish between his own property and that of the innocent party.²³

23. *Smith v. Mottley*, 17 A. B. R. 866, 150 Fed. 266 (C. C. A. Ohio).

Laches bars right to trace: If the owners of trust funds are guilty of laches in asserting their rights, they will be denied the right to disturb distribution, or to relief in lieu of restitution.

In *re Wilkesbarre Furn. Mfg. Co.*, 12 A. B. R. 472, 130 Fed. 796 (D. C. Penn.), which was the case of a partner, misappropriating firm assets to make good a shortage in his accounts as trustee in bankruptcy; firm creditors guilty of laches in not attempting to identify and trace the appropriate assets nor to stay distribution pending the determination of a petition filed against firm; firm creditors cannot come upon the lienholders' share of the proceeds on the ground that the lienholder has received a preference; the preference is recoverable only at the suit of the trustee and the firm creditors have no prior right to any recovery thereof.

Clafin Dry Goods Co. v. Eason, 2 A. B. R. 263 (Ref. Tex.).

Interest.—Interest may be allowed in some instances, as where the trust funds were tortiously converted, *Hutchinson v. Otis*, 8 A. B. R. 392, 115 Fed. 937 (C. C. A. Mass.): "In *Hutchinson v. LeRoy* (C. C. A.), 8 Am. B. R. 20, 113 Fed. 202, already referred to, we allowed interest against the petitioner; but there the fund which it was determined belonged to him, had been held adversely from the outset, as it grew out of a tort of the bankrupt which arose before proceedings in

bankruptcy were commenced. In the present case, however, the fund came into the hands of the trustee in bankruptcy, not through any tort, but through the oversight of *Otis, Wilcox & Co.* The trustee merely held it until the courts could determine to whom it belonged, and the record does not show that the trustee has received any increment thereof."

Costs and Expenses.—A proportionate part of the costs and expenses may be charged against the owner of the trust fund and deducted from the amount of the fund decreed to belong to him, *In re Gaskill*, 12 A. B. R. 251, 130 Fed. 235 (D. C. Wash.); contra, *Smith v. Township*, 17 A. B. R. 750, 150 Fed. 257 (C. C. A. Mich.).

Remand for Further Proof as to Identity of Proceeds.—Where it appears that some, at least, of the goods came into the custody of the court the case may be remanded to take further proof to fix the amount of the equitable lien, *Erie R. R. Co. v. Dial*, 15 A. B. R. 559, 140 Fed. 689 (C. C. A. Ohio).

Agreement to Give Mortgage on Receipt of Goods Disregarded and Goods Commingled.—Where a bankrupt disregards an agreement to give a mortgage on receipt of goods purchased, and commingles the goods with his own, the seller has a lien on the whole, *In re Hennis*, 17 A. B. R. 889 (Ref. N. Car.).

Compare, *Smith v. Township*, 17 A. B. R. 545, 150 Fed. 257 (C. C. A. Mich.).

In re Acheson Co., 22 A. B. R. 338, 170 Fed. 427 (C. C. A. Ore.): "In carrying out the rule when it comes to proof, the owner must assume the burden of ascertaining and tracing the trust funds, showing that the assets which have come into the hands of the trustee have been directly added to or benefited by an amount of money realized from the sales of the specific goods held in trust; and recovery is limited to the extent of this increase or benefit. * * * If, however, he succeeds in making requisite proof, it then devolves upon the bankrupt, or the trustee who takes the property of the bankrupt, in the same relation that it was held by the bankrupt, to distinguish between what is his and that of the cestui que trust. We do not mean to be understood as holding that equity will grant to a cestui que trust relief against any assets in the hands of a trustee, for it will not go farther than to give a lien when the facts are that there remain in the estate specific funds or property which have increased the assets of the estate, and which represent the proceeds of the specific property intrusted to the bankrupt. *Lowe v. Jones*, Adm'r, 192 Mass. 94, 78 N. E. 402, 6 L. R. A. (N. S.) 487, 116 Am. St. Rep. 225. Moreover, if there has been expenditure, and the funds are gone, and no specific property or money is found instead of the funds, it is inequitable that some other property found should be applied to pay one creditor in preference to another. So, funds that have been dissipated or that have been used to pay other creditors, or that have been spent to pay current business expenses, are not recoverable, because they are gone, and there is nothing remaining to be the subject of the trust. This qualification of the general rule is to be applied to the facts pleaded in the present case, inasmuch as it is alleged that some of the trust moneys were used by the bankrupt in paying its employees, and in the expenses of running its business, and in paying other creditors. For them there can be no recovery."

And in bankruptcy, the trustee stands in such cases in the bankrupt's shoes, and the case is different from that of seizure by creditor's bills.

Smith v. Mottley, 17 A. B. R. 866, 150 Fed. 266 (C. C. A. Ohio): "Again, if the trustee takes the bankrupt's property in the same plight as the bankrupt held it, and while the bankrupt held the assets, they became subject to a lien upon the mass, which was not destroyed by its continual transformation in business from day to day, the paying out and receiving in, of parcels of the fund, and no creditor having levied upon it, or the right of an innocent party fastened upon it, it is difficult to see how by the succession of the trustee the lien could be lost. Whether it was a lien or not would continue to be the same question as it was between the bankrupt and the owner of the misappropriated fund.

"There would seem to be a valid distinction in the application of the rule that the misappropriated fund must be found in the assets, between the settlement of an estate in bankruptcy proceedings and proceedings upon a bill filed for the marshaling and appropriation of assets according to the principles of equity. In the latter case there is a seizure of the res for the direct purpose of fastening the inchoate rights of creditors."

§ 1884¹/₄. **Evidence.**—Possession is itself evidence raising the presumption of ownership.²⁴ Uncontradicted testimony may yet be rejected if improbable.²⁵

²⁴ In re Mayer, 19 A. B. R. 480, 156 Fed. 432, 157 Fed. 836 (D. C. Pa.), quoted at § 554¹/₂; In re Diamond, 19

A. B. R. 811, 158 Fed. 370 (D. C. Ala.).
²⁵ See ante, §§ 554, et seq., also post, §§ 2646, 2650, et seq., or if acces-

§ 1884½. Goods in Warehouse or Elevator, and Outstanding Receipts.—Where goods are in a warehouse or grain in an elevator on the bankrupt's premises, and receipts or certificates have been issued therefor, the rights of the parties in the absence of fraud are to be determined by state law.²⁶ If by state law title has passed, and there be no fraud, then in bankruptcy the title will not be in the trustee.²⁷

However, if there be fraud, then, since the Bankruptcy Act, in § 70 (a), passes to the trustee title to all property fraudulently transferred, the trustee will get title,²⁸ even though the fraud be "fraud in law" without intentional bad faith.²⁹

Where parts of the goods or grain have been converted, the rules of § 1884 prevail; thus, where subsequent additions to the common stock have been made.³⁰

§ 1884¾. Costs and Expenses on Reclamation or on Surrender of Trust Funds.—Before the Amendment of 1910 granting commissions to trustees and receivers "on all moneys disbursed or turned over to any person, including lienholders, by them," etc., it had been ruled that neither the trustee, referee, nor receiver could be allowed compensation out of property surrendered to adverse claimants.³¹

Gillespie v. Piles, 24 A. B. R. 502, 178 Fed. 886 (C. C. A. Iowa): "The court ordered that out of the proceeds of the hogs there should be paid to the referee and trustee the percentages specified in these sections of the Bankruptcy Law. But these proceeds were no part of the estate of the bankrupt, and they could not be "administered" as such before the referee or by the trustee. They were the property of the interveners, which the trustee had obtained possession of through the fraud of the bankrupt, and which it was his duty to return to the interveners immediately upon their rescission of the sales and their demand for the property. The latter were not creditors of the estate. The proceeds here in question were not distributable to the creditors of the estate or to the creditors of Hough. They were the property of the interveners, and the direction that these percentages should be paid to the referee and the trustee out of these proceeds cannot be sustained. Property which comes to the possession of a trustee in bankruptcy through the fraud of the bankrupt, and is adjudged to be returned to the victim of the fraud, is not a part of the estate of the

sible witnesses are not produced in corroboration. In *re Mayer*, 19 A. B. R. 480, 156 Fed. 432, 157 Fed. 836 (D. C. Pa.), quoted at § 554½; In *re Baumhauer*, 24 A. B. R. 753, 179 Fed. 966 (D. C. Ala.), quoted at § 852.

²⁶ See ante, § 1146. But compare, § 964.

²⁷ Compare. In *re Millbourne Mills Co.*, 20 A. B. R. 146, 162 Fed. 988 (D. C. Pa.), wherein the court held that where grain is commingled in an elevator and there are outstanding warehouse certificates, nevertheless the grain passes to the trustee in bankruptcy.

²⁸ See ante, § 1146; also, (*Security Warehouse Co. v. Hand*, 19 A. B. R. 291, 206 U. S. 415.

²⁹ In *re Standard Tel. & Elec. Co.* (*Knapp v. Milw. Tr. Co.*), 24 A. B. R. 761, 216 U. S. 545, quoted at §§ 1207¼ and 1285.

³⁰ In *re Brown & Co.*, 22 A. B. R. 659, 171 Fed. 281 (D. C. N. Y.).

³¹ Bankruptcy Act as Amended 1910, § 48. Compare, successful claimant of trust funds refused costs and expenses out of bankrupt assets, In *re Stewart*, 24 A. B. R. 414, 178 Fed. 463 (D. C. N. Y.).

bankrupt, and the referee and trustee may not be allowed their statutory percentages out of it."

But, on principle, there is to be noted a radical difference between the allowance of compensation to the trustee or receiver for services in the care of the assets impounded pending the determination of the rights of the parties therein, as also of the referee in adjudicating the rights of the parties therein, and the allowance of compensation therefrom to an attorney for the receiver or trustee in endeavoring, in behalf of unsecured creditors, to defeat the owner's claim. Certainly it is to be conceded that one whom the court has determined to be the rightful owner of property should not be compelled to pay his opponent's attorneys' fees incurred in the ineffectual effort to keep him out of his property. But it has ever been the recognized rule that a court officer in charge of property in dispute in a court of equity may have his expenses and compensation therefrom for his care of it, as also that the court may have therefrom that portion of its own costs assignable to that particular controversy. The failure to distinguish the dual capacity of the trustee in bankruptcy, noted ante, at § 896, as being on the one hand a party litigant, as "owner" and agent of the general creditors, and as being on the other hand a court officer, holding and caring for the property of all to await the determination of the rights of the parties therein, strikes the line of demarkation and affords a reasonable basis of distinction. In bankruptcy administration there arise frequent instances of the tracing of funds alleged to be trust funds and of the reclamation of property claimed, not seldom under doubtful title, by others. Such adverse claimants would be under the necessity of resorting to some court to establish their rights in any event; and if they are compelled to use the forum of the bankruptcy court for such purpose it should not exonerate them from all charge nor compel trustees and referees to protect the property of such claimants and determine their rights gratuitously.

It was in recognition of this manifest injustice to the court officers in bankruptcy that Congress in the Amendment of 1910 permitted the courts, in their discretion, to allow commissions, not to exceed the certain limited rates specified, to trustees and receivers "on all moneys disbursed or turned over to any person, including lienholders, by them," etc.³²

Of course the court, in its discretion, may refuse compensation, for § 48 as amended simply establishes an outside limit upon the discretion of the court in making allowances and does not attempt at all to control that discretion within those limits.

But it is still the rule, and must always be the rule, that reimbursement should not be allowed out of the rightful owners property for the attorneys'

32. *Smith v. Township*, 17 A. B. R. 750, 150 Fed. 257 (C. C. A. Mich.); contra, and to the effect that a proportionate part of the costs and expenses may be charged against the

owner of a trust fund and deducted from the fund decreed to him, see *In re Gaskill*, 12 A. B. R. 251, 130 Fed. 235 (D. C. Wash.).

fees and other expenses or even for the compensation of the trustee or receiver incurred as a party litigant in opposing the claims of rightful owners.

Gillespie v. Piles, 24 A. B. R. 502, 178 Fed. 886 (C. C. A. Iowa): "There is a manifest injustice and inequity in taking out of a fund or property in the custody of a court compensation for the services of an attorney or for the service of any other party by means of which the fund or property has been taken or kept from its true owner. The latter ought not to be required to pay for services which have been a positive detriment to him. And courts of equity may not lawfully take out of a fund or property in its custody and pay compensation for the services of an attorney of a trustee or for the services of any other party by means of which the fund or property has been taken or detained from its equitable owner. *Hobbs v. McLean*, 117 U. S. 567, 581, 6 Sup. Ct. 870, 29 L. Ed. 940."

DIVISION 5.

MARSHALING OF LIENS ON PROPERTY IN THE CUSTODY OF THE BANKRUPTCY COURT.

§ 1885. **Jurisdiction to Marshal Liens.**—Liens upon, and interests in, the property in the custody of the bankruptcy court may be marshaled and their validity and priority determined by the bankruptcy court, in the bankruptcy proceedings.³³

33. See ante, "Summary Jurisdiction of the Bankruptcy Court," §§ 1794, 1795. See post, "Selling Property Free from Liens," § 1965, et seq.

In re *Sentenne & Green Co.*, 9 A. B. R. 648, 120 Fed. 436 (D. C. N. Y.), quoted at § 1795. In re *Pittelkow*, 1 A. B. R. 472, 92 Fed. 901 (D. C. Wis.), quoted at § 1795. In re *New England Piano Co. (Union Trust Co.)*, 9 A. B. R. 767, 122 Fed. 937 (C. C. A. Mass.); In re *McMahon*, 17 A. B. R. 532, 147 Fed. 648 (C. C. A. Ohio); *obiter*, *Whitney v. Wenham*, 14 A. B. R. 45, 198 U. S. 539; In re *Porterfield*, 15 A. B. R. 18, 138 Fed. 192 (D. C. W. Va., reversed, on other grounds, sub nom. *Moore v. Green*); *impliedly*, *Ludowici Roofing Tile Co. v. Penn. Inst.*, 8 A. B. R. 742 (D. C. Penn.); In re *Emslie*, 4 A. B. R. 126, 102 Fed. 292 (C. C. A. N. Y.); In re *Pratesi*, 11 A. B. R. 319, 126 Fed. 588 (D. C. Del.); In re *Rodgers*, 11 A. B. R. 89, 125 Fed. 169 (C. C. A. Ills.); In re *Southern Loan & Trust Co. v. Benbow*, 3 A. B. R. 10, 96 Fed. 514 (D. C. N. Car., reversed sub nom. *Frazier v. Southern Loan & Trust Co.*, 3 A. B. R. 710, 99 Fed. 707); *obiter*, In re *Cobb*, 3 A. B. R. 130, 96 Fed. 821 (D. C. N. Car.); *Havens & Geddes Co. v. Pierek*, 9 A. B. R. 569, 120 Fed. 244 (C. C. A. Ills.); In re *Lem-*

mon & Galé Co., 7 A. B. R. 291, 112 Fed. 296 (C. C. A. Tenn.); In re *Prince and Walter*, 12 A. B. R. 678 (D. C. Penn.); In re *Worland*, 1 A. B. R. 450, 92 Fed. 893 (D. C. Iowa); In re *Antigo Screen Door Co.*, 10 A. B. R. 359, 123 Fed. 249 (C. C. A. Wis.); In re *Groetzing*, 11 A. B. R. 723, 127 Fed. 814 (C. C. A. Penn.); In re *Wilka*, 12 A. B. R. 727, 131 Fed. 1004 (D. C. Iowa, affirmed sub nom. In re *Granite City Bk.*, 14 A. B. R. 404, 137 Fed. 818, C. C. A.); In re *Noel*, 14 A. B. R. 715, 137 Fed. 694 (D. C. Md.); *inferentially*, *Carriage Co. v. Solanas*, 6 A. B. R. 221, 108 Fed. 532 (D. C. La.); *inferentially*, In re *Schloerb*, 3 A. B. R. 224, 97 Fed. 326 (D. C. Wis., affirmed sub nom. *White v. Schloerb*, 4 A. B. R. 178, 178 U. S. 542); In re *McCallum*, 7 A. B. R. 596, 113 Fed. 393 (D. C. Penn.); *obiter*, In re *Corbett*, 5 A. B. R. 224, 104 Fed. 872 (D. C. Wis.); *inferentially*, In re *Drayton*, 13 A. B. R. 602, 135 Fed. 883 (D. C. Wis.).

Instances, In re *Waterloo Organ Co.*, 9 A. B. R. 429, 118 Fed. 904 (D. C. N. Y.); In re *Myers*, 4 A. B. R. 536, 102 Fed. 869 (D. C. Penn.); In re *Reliance Storage & Warehouse Co.*, 5 A. B. R. 249 (D. C. Pa.); In re *Dunavant*, 3 A. B. R. 41, 96 Fed. 542 (D. C. N. Car.); In re *Hugill*, 3 A. B. R. 686,

In re Rochford, 10 A. B. R. 608, 124 Fed. 182 (C. C. A. S. Dak.): "The District Court sitting in bankruptcy has jurisdiction to determine, after reasonable notice to the claimants to present their claims to it, the claims of all parties to property and to the proceeds of property which its officers have lawfully reduced to their actual possession in the course of the administration of the estate of the bankrupt, and controversies between trustees in bankruptcy and adverse claimants to property which has in this way reached the custody of the District Courts are not controversies at law or in equity, as distinguished from proceedings in bankruptcy, within the proper interpretation of § 23."

Chauncey v. Dyke Bros., 9 A. B. R. 444, 119 Fed. 1 (C. C. A. Ark., affirming In re Matthews, 6 A. B. R. 96): "But if, in the exercise of its customary jurisdiction, the bankrupt court obtained the lawful custody of the res to which the liens related or of a fund realized from its sale, then the duty which was thereby devolved upon it, of distributing the fund among those to whom it rightfully

100 Fed. 616 (D. C. Ohio); In re Bartheleme, 11 A. B. R. 67 (Ref. N. Y.); In re Rude, 4 A. B. R. 319, 101 Fed. 805 (D. C. Ky.); McNair v. McIntyre, 7 A. B. R. 638, 113 Fed. 113 (C. C. A. N. Car.); Long v. Gump, 16 A. B. R. 501 (C. C. A. Ohio); Morgan v. Nat'l Bk., 16 A. B. R. 639, 145 Fed. 466 (C. C. A. W. Va.); In re Moore, 17 A. B. R. 164 (D. C. Ga.); Smith v. Township, 17 A. B. R. 747 (C. C. A. N. J.); O'Dell v. Boyden, 17 A. B. R. 759, 150 Fed. 731 (C. C. A. Ohio); Ryttenburg v. Schefer, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.); In re L'Hommedieu, 16 A. B. R. 850 (C. C. A. N. Y.); In re McIntire, 16 A. B. R. 80 (D. C. W. Va.). Instance, and obiter, In re Cramond, 17 A. B. R. 31, 145 Fed. 566 (D. C. N. Y.); Ommen v. Talcott, 26 A. B. R. 689, 188 Fed. 401 (C. C. A. N. Y.); instance, lien of judgment on after-acquired property superior to lien of mortgage subsequently executed, In re Pritchard, 27 A. B. R. 238, 192 Fed. 736 (D. C. Pa.); In re Schermerhorn, 16 A. B. R. 509, 145 Fed. 341 (C. C. A.).

Instances:

(1) Chattel Mortgages.—In re Sentenne & Green Co., 9 A. B. R. 648, 120 Fed. 436 (D. C. N. Y.); In re Rochford, 10 A. B. R. 608, 124 Fed. 182 (C. C. A. S. Dak.).

(2) Mechanics' liens or rights under building contracts. In re Emslie, 4 A. B. R. 126, 102 Fed. 292 (C. C. A. N. Y.); Chauncey v. Dyke Bros., 9 A. B. R. 444, 119 Fed. 1 (C. C. A. Ark.); Ludowici Tile Roofing Co. v. Penn. Inst., 8 A. B. R. 742 (D. C. Pa.); In re Farmers Supply Co., 22 A. B. R. 460, 170 Fed. 502 (D. C. Ohio).

(3) Relative priorities of mechanics' liens and bonded indebtedness of a plant, Morgan v. Nat'l Bk., 16 A. B. R. 639, 145 Fed. 466 (C. C. A. W. Va.); In

re Clark Coal & Coke Co., 23 A. B. R. 273, 173 Fed. 658, 176 Fed. 955 (D. C. Pa.).

(4) Subcontractors not filing liens as against valid assignments of portions of fund to bank advancing money to contractor. In re Cramond, 17 A. B. R. 22, 145 Fed. 566 (D. C. N. Y.).

(5) Usurious lien agreement. Ryttenburg v. Schefer, 11 A. B. R. 652, 131 Fed. 313 (D. C. N. Y.). But see, In re Holmes Lumber Co., 26 A. B. R. 119, 189 Fed. 178 (D. C. Ala.).

(6) Assignment of interest in estate to secure usurious claim. In re L'Hommedieu, 16 A. B. R. 850 (C. C. A. N. Y.).

(7) Mortgage on bankrupt's real estate tainted with usury. In re Kellogg, 10 A. B. R. 11, 121 Fed. 333 (C. C. A. N. Y.).

(8) Deed of trust to wife in consideration of surrender of dower. In re Porterfield, 15 A. B. R. 18, 138 Fed. 192 (D. C. W. Va.).

(9) Attorney's lien upon dividends coming to client for services in successfully prosecuting the claim in the bankruptcy court. In re Rude, 4 A. B. R. 519, 101 Fed. 805 (D. C. Ky.).

(10) Execution creditors holding under levies made more than four months prior to bankruptcy—contending that prior lien by way of trust deed, was fraudulent. In re Dunavant, 3 A. B. R. 41, 96 Fed. 542 (D. C. N. Car.).

(11) Landlord, no lien for unpaid rent accruing after adjudication, in Louisiana, because chattels not on premises with express or implied consent of owner after levy. Carriage Co. v. Solanas, 6 A. B. R. 221, 108 Fed. 532 (D. C. La.).

(12) Landlord's priority over liens acquired after tenancy began. In re McIntire, 16 A. B. R. 80 (D. C. W. Va.).

(13) Real estate in one partner's name, whether firm assets. In re

belonged, did empower it to determine the relative priorities of the conflicting claims to the fund. A court which has lawfully acquired the custody of property or money must of necessity dispose of the same according to law; and, when conflicting claims are preferred, it is not bound to require the claimants to litigate their claims in some other forum, and to adopt the judgment of that tribunal, although it may do so, but it is at liberty to dispose of such controversies according to its own ideas of right and justice. This is one of those incidental powers which may be exercised by any court of record in the absence of an express prohibition."

Burleigh v. Foreman, 11 A. B. R. 75, 125 Fed. 217 (C. C. A. Mass.): "Section 2 * * * enumerates certain matters over which the courts of bankruptcy are invested with the jurisdiction at law and in equity. This gives them undoubted cognizance of the marshaling of assets in the possession of the trustee in proceedings like that underlying this appeal."

In *re Dana*, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.): "The principal question

Groetzinger, 11 A. B. R. 723, 127 Fed. 814 (C. C. A. Penn.).

(14) Taxes on merchandise sold in bulk becoming a lien while in the custody of the bankruptcy court before sale. In *re Keller*, 6 A. B. R. 351, 109 Fed. 131 (D. C. Iowa).

(15) Compelling resort to execution against personal property of other parties before enforcing lien on real estate of bankrupt. In *re Pollman*, 16 A. B. R. 146 (Ref. N. Y.).

(16) Partial assignments of building contract fund turned over by owner to bankruptcy court for administration. In *re Ludowici Roofing Tile Co.* *v. Penn. Inst.* 8 A. B. R. 742 (D. C. Penn.).

(17) Liquor license: Bankrupt claiming liquor license not his own although in his own name but simply being used in wife's business. In *re Emrich*, 4 A. B. R. 91, 101 Fed. 231 (D. C. Pa.).

(18) Township's claim of lien by way of commingled trust funds, *Smith v. Township*, 17 A. B. R. 747 (C. C. A. N. J.).

(19) Liens and prior assignments upon seat in stock exchange. *O'Dell v. Boyden*, 17 A. B. R. 759, 150 Fed. 731 (C. C. A. Ohio).

(20) Landlord's lien under distress warrant. In *re Lines*, 13 A. B. R. 318, 133 Fed. 803 (D. C. Penn.).

(21) Landlord no priority out of proceeds of liquor license because license not subject to levy. In *re Myers*, 4 A. B. R. 536, 102 Fed. 869 (D. C. Penn.).

(22) Mortgage lien of bank where claim made that the loan was void as exceeding charter rights. *Cunningham v. Germ. Ins. Bk.*, 4 A. B. R. 365, 103 Fed. 932 (C. C. A. Ky.).

(23) Factor's lien for advances, commissions and expenses, where factor

is not in possession. *Ryttenberg v. Schefer*, 11 A. B. R. 652, 150 Fed. 731 (C. C. A. Ohio).

(24) Whether novation was made on purchaser of plant taking up old mortgage and giving new mortgage covering more. *Long v. Gump*, 16 A. B. R. 501 (C. C. A. Ohio). Compare (reorganized corporation composed of bondholders and directors, buying in assets and accepting bonds and stocks of new company), In *re Medina Quarry Co.*, 24 A. B. R. 769, 179 Fed. 929 (D. C. N. Y.).

(25) Novation—None exists where bankrupt deeds to his father real estate encumbered with a mortgage made to secure the note of the bankrupt where father devises real estate back to bankrupt and bankrupt's sister. In *re Straub*, 19 A. B. R. 808, 153 Fed. 375 (D. C. W. Va.).

(26) Liveryman's lien, In *re Pratesi*, 11 A. B. R. 319, 126 Fed. 588 (D. C. Del.).

(27) Division of proceeds of insurance policy among creditors in accordance with previous agreement. In *re Reliance Storage & Warehouse Co.*, 5 A. B. R. 249 (D. C. Penn.).

(28) Rent of mortgaged premises accruing after adjudication, or accruing beforehand but uncollected or still in the bankrupt's hands. In *re Cass*, 6 A. B. R. 722 (Ref. Ohio); In *re Dole*, 7 A. B. R. 21, 101 Fed. 926 (D. C. Vt.). Compare, to same effect, In *re Hollenfeltz*, 2 A. B. R. 499, 94 Fed. 629 (D. C. Iowa).

(29) Mortgages. In *re Pittelkow*, 1 A. B. R. 472, 92 Fed. 901 (D. C. Wis.); In *re Noel*, 14 A. B. R. 715, 137 Fed. 674 (D. C. Md.); *Carter v. Hobbs*, 1 A. B. R. 214, 92 Fed. 594 (D. C. Ind.); In *re Wilka*, 12 A. B. R. 727, 131 Fed. 1004 (D. C. Iowa); *McNair v. McIntyre*, 7 A. B. R. 638, 113 Fed. 113 (C.

arising on this petition to revise is whether a District Court of the United States, in which bankruptcy proceedings are pending, and which is in the actual possession of certain real estate conceded to belong to the bankrupt, has jurisdiction to determine the amount and the order of priority of liens thereon, and to liquidate such liens, to the end that the property may be sold free of incumbrances and in aid thereof to enjoin the lienholders from prosecuting the foreclosure of their liens in a suit brought in a State court before the commencement of the bankruptcy proceedings but within four months thereof; and this, though the lienholders object to such jurisdiction, and it is not contended that their liens are preferential or fraudulent or invalid for any other reason. Bearing in mind the property was the property of the bankrupt, the title to which had passed to the trustee in bankruptcy, and that it was in the actual possession of the District Court of the United States, we think an affirmative answer should be given, upon the authority of *In re Schermerhorn*, *In re Epstein* (quoted § 1797) and the cases therein cited. * * * Indeed, it appears

C. A. N. C.); *In re Prince & Walter*, 12 A. B. R. 678 (D. C. Penn.); *In re Bartheleme*, 11 A. B. R. 67 (Ref. N. Y.), mortgage alleged to be fraudulent; *In re Hugill*, 3 A. B. R. 686, 100 Fed. 616 (D. C. Ohio): Mortgage void for actual fraud as to part, void as to whole.

(30) Judgments. *In re L'Hommedieu*, 16 A. B. R. 850 (C. C. A. N. Y.).

(31) Deed given by way of security: *In re Moore*, 17 A. B. R. 164 (D. C. Ga.).

(32) Transfer of stock under forged powers of attorney, *Unity Banking & Sav. Co. v. Boyden*, 20 A. B. R. 264, 159 Fed. 916 (C. C. A. Ohio).

Misuse of life insurance policies surrendered by children to father for specific purpose, liens marshaled; subrogation to real estate mortgage lien consequent thereon, *In re MacDougall*, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.).

(33) Bankrupt assumes mortgage, on purchase of property; another collateral mortgage given by same debtor for same debt, foreclosed; mortgagee to resort first to bankrupt's property, *In re Beaver Knitting Mills*, 18 A. B. R. 528, 154 Fed. 320 (C. C. A. N. Y.).

(34) Fraudulently transferred real estate, where bankrupt still in occupancy, though claiming another owns it, *In re Coffey*, 19 A. B. R. 148 (Ref. N. Y.).

(35) Goods in warehouse on bankrupt's premises for which warehouse receipts issued, (*Security Warehousing Co. v. Hand*, 19 A. B. R. 291, 206 U. S. 415. See §§ 964, 1146, 1884½.

(36) Grain in storage on bankrupt's premises for which certificate issued, *In re Millbourne Mills Co.*, 20 A. B. R. 746, 162 Fed. 988 (D. C. Pa.), quoted at §§ 964, 1146, 1884½; Fourth

St. Nat. Bank *v. Millbourne Mills Co.*, 22 A. B. R. 442, 172 Fed. 177 (C. A. Pa.).

(37) Maritime liens on cargo and receiver's certificates for care and preservation, *In re Alaska Fishing, etc., Co.*, 21 A. B. R. 685, 167 Fed. 875 (D. C. Wash.).

(38) Deeds of trust that had been inadvertently or fraudulently released decreed to be reinstated and the rights of the holders of notes secured thereby protected by declaring their right to a lien on said real estate, *Dulany v. Waggaman*, 22 A. B. R. 36 (Sup. Ct. D. C.).

(39) Misdescription of mortgage debt, *In re Farmers Supply Co.*, 22 A. B. R. 460, 170 Fed. 502 (D. C. Ohio).

(40) Corporate seal lacking, *In re Farmers Supply Co.*, 22 A. B. R. 460, 170 Fed. 502 (D. C. Ohio).

(41) Alteration of mortgage bond to cover new indebtedness subsequently created between same parties, *In re Burns*, 22 A. B. R. 640, 171 Fed. 1008 (D. C. Ga.).

(42) Auctioneer's lien for advancements made to bankrupt before bankruptcy. *In re Corn*, 24 A. B. R. 681, 179 Fed. 841 (C. C. A. N. Y.).

(43) Dower in cases of purchase money mortgage, whether computed on surplus or on entire value, in Ohio. *In re Hays*, 24 A. B. R. 669, 181 Fed. 674 (C. C. A. Ohio).

(44) Mortgage, set up by intervening petition, declared void for permitting mortgagor to remain in possession and to sell, though intentional bad faith absent, in *In re Standard Tel. & Elec. Co. (Knapp v. Milw. Tr. Co.)*, 24 A. B. R. 761, 216 U. S. 545, quoted at §§ 1207¼ and 1258.

(45) Conditional vendor praying for marshaling of liens and payment of the

that before the injunction in question was awarded, the State court, which by its receiver had actual possession of the property, voluntarily surrendered it to the receiver appointed in the bankruptcy proceedings upon request being made."

In re Granite City Bk., 14 A. B. R. 408, 137 Fed. 818 (C. C. A. Iowa): "* * * he can assert his rights to the proceeds before the referee, when and where his claim can be heard and its priority be determined."

In re Kellogg, 10 A. B. R. 11, 121 Fed. 333 (C. C. A. N. Y.): "The second assignment of error raises the question as to the power of the bankruptcy court to determine the question of the validity and amount of said bond and mortgage in the summary proceedings instituted before the referee in bankruptcy. Did the bankruptcy court, after having acquired actual possession and control of the property, have power to determine the validity of the liens thereon? * * * It must be held that the bankruptcy court, upon such acquisition by the receiver of possession and undisputed legal title, had jurisdiction to determine the validity of the mortgage."

Carter v. Hobbs, 1 A. B. R. 215, 92 Fed. 594 (D. C. Ind.): "From the foregoing considerations it would seem to be clear that the District Court when sitting in bankruptcy has lawful jurisdiction over liens and mortgages upon the property of the bankrupt, so that it may inquire into their validity and extent and grant the same relief which the courts of the State might or ought to grant, and that such court may do this without the consent of the secured creditor."

Impliedly, In re Pollman, 16 A. B. R. 146 (Ref. N. Y.): "The court of bankruptcy having possession of the property in question, must administer the same in accordance with the equitable principles of the Bankruptcy Act. * * * Thus the court will compel the creditor to resort first to the unsold portion of real estate before going to that which the debtor has alienated. * * * Incident to this system, which supersedes all other systems of administering insolvent estates, secured creditors will often be compelled to submit to delay, if delay is likely to benefit the creditors at large. In re Sabine, 1 Am. B. R. 315, 321. Stays of legal proceedings are constantly granted, and the bankruptcy court will so regulate the time and manner of enforcement of valid liens, as not to cause unnecessary loss to others. In re Baughman, 15 Am. B. R. 23, 138 Fed. 742; In re Vastbinder, 13 Am. B. R. 148, 132 Fed. 718; In re Chambers, 3 Am. B. R. 537, 98 Fed. 865."

Inferentially, In re Moody, 12 A. B. R. 724, 131 Fed. 525 (D. C. Iowa): "It is a familiar principle of equity jurisprudence that property in the custody of a court of equity is always held by it in trust for those to whom it rightly belongs; and the jurisdiction to inquire into and determine to whom it so belongs, and to that end to require all claimants thereto to present their claims within

balance of his purchase price as an equitable lien, rather than asking for surrender of the property itself. In re Max Goldman, 23 A. B. R. 497, 174 Fed. 579 (C. C. A. Ohio), quoted at § 1878.

(46) Reformation of second mortgage to be a first lien on another piece of property. Hardy v. Chandler, 23 A. B. R. 717, 175 Fed. 138 (D. C. Ga.).

(47) Exempt Property.—It has been held that a creditor holding lien on both exempt and non-exempt property, need not exhaust security on exempt property first. In re Bailey, 24

A. B. R. 201, 176 Fed. 990 (D. C. Utah).

(48) Contribution, Where Stock Jointly Pledged with Other Stock as Collateral but Loan Entirely Satisfied Out of Proceeds of the Other Stock.—In re McIntyre & Co., 24 A. B. R. 626, 181 Fed. 955 (C. C. A. N. Y.).

(49) Mortgagor cutting timber, where description copied into mortgage recites right of ingress and egress to cut timber. In re Holmes Lumber Co., 26 A. B. R. 119, 189 Fed. 178 (D. C. Ala.).

a stated time, or be barred of any interest in or right to the property, is inherent in every court of equity."

Thus, the bankruptcy court may determine whether a transfer or conveyance by the bankrupt of property still remaining in the possession of the bankruptcy court, is fraudulent or preferential.³⁴

The bankruptcy court need not sell merely whatever title the trustee has and leave the purchaser to litigate, afterwards, the extent of it, but may determine its extent and validity in the first instance;³⁵ and may determine in advance of the sale of a leasehold the rights of the landlord under a forfeiture clause.³⁶

§ 1886. Consent of Lienholder Not Necessary.—The consent of the lienholder is not necessary.³⁷

§ 1887. Incidental Power to Compel Execution of Papers by Third Parties.—As incident to the power, undoubtedly the bankruptcy court has jurisdiction to order the surrender or cancellation of instruments affecting the property so in its custody; but not by service of process upon persons outside of the district.³⁸ And it has jurisdiction to order the execution of assignments;³⁹ but power to compel a pledgor to execute necessary papers to effect a sale of the pledged property, where the pledged property was in the bankrupt's possession, has been denied.⁴⁰

Where a wife has given her consent to the sale of real estate free from her dower interest and to accept the money value in lieu thereof, she may be compelled to execute a formal release of her dower right.

In *re Acretelli*, 21 A. B. R. 537, 173 Fed. 121 (D. C. N. Y.): "The right to make the sale presupposes the power to compel it, the consent once given."

§ 1887 $\frac{1}{4}$. Incidental Power to Reform Instruments.—Also as incident to the power, the bankruptcy court undoubtedly has jurisdiction to reform instruments, where a proper case for reformation exists.⁴¹

³⁴. In *re Coffey* 19 A. B. R. 148 (Ref. N. Y.); also cases cited ante, this same paragraph.

³⁵. [1867] *Ray v. Norseworthy*, 23 Wall. 128; inferentially, In *re Waterloo Organ Co.*, 9 A. B. R. 427, 118 Fed. 904 (D. C. N. Y.); In *re McBride & Co.*, 12 A. B. R. 83, 132 Fed. 285 (Ref. N. Y.); [1841] In *re Christy*, 3 How. (U. S.) 292; In *re Sanborn* 3 A. B. R. 54, 96 Fed. 507 (D. C. Vt.); [1841] *Houston v. Bank*, 6 How. 486.

³⁶. *Gazlay v. Williams*, 17 A. B. R. 249 (C. C. A. Ohio).

³⁷. See post, "Selling Property Free from Liens," § 1966. But compare, In *re Durham*, 8 A. B. R. 115, 114 Fed. 750 (D. C. Md.), where the court evidently deemed his consent necessary. See, also, In *re Kohl-Hepp Brick Co.*, 23 A. B. R. 822, 176 Fed. 340 (C. C.

A. N. Y.), quoted at §§ 1970, 1980; In *re Dana*, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.), quoted at § 1885.

Whether conditional sale contract to be considered "lien," from which property may be sold clear and free, see In *re Grainger*, 20 A. B. R. 166, 160 Fed. 69 (C. C. A. Calif.).

³⁸. In *re Waukesha Water Co.*, 8 A. B. R. 715, 116 Fed. 1009 (D. C. Wis.). Compare, In *re Harris*, 23 A. B. R. 237, 173 Fed. 735 (D. C. N. Y.), as to lack of power where person outside of district also, see ante, § 29.

³⁹. In *re Bacon*, 12 A. B. R. 732, 132 Fed. 157 (D. C. N. Y.).

⁴⁰. In *re Silberhorn*, 5 A. B. R. 568, 105 Fed. 809 (D. C. Ills.).

⁴¹. *Fowler v. Hart*, 13 How. 373. But compare, *Sexton v. Kessler*, 21 A.

§ 1887½. **And to Relieve against Forfeiture.**—Also the bankruptcy court undoubtedly has the incidental power to relieve against forfeiture, which it will exercise under the usual equity rules.⁴²

§ 1888. **Referee Has Jurisdiction.**—The referee has jurisdiction to marshal liens and to determine their extent, validity and order of priority.⁴³

In re Rochford, 10 A. B. R. 608, 124 Fed. 182 (C. C. A. S. Dak.): "A referee in bankruptcy has jurisdiction to draw to himself by summary process or notice, and in the first instance to determine the question of the validity of the claim of a third party to a lien upon it, or an interest in, property or the proceeds of property lawfully in the custody of a trustee in bankruptcy."

Mound Mines Co. v. Hawthorne, 23 A. B. R. 242, 173 Fed. 882 (C. C. A. Colo.): "Where, however, property which is in the possession of a bankrupt at the time of the bankruptcy proceedings, and passes as part of his estate into the possession of the trustee in bankruptcy, and a third party claims an interest therein, the referee may, by a summary proceeding, require such third party to appear in the bankruptcy court, present his claim, and the referee adjudicate the rights of the parties in respect thereof."

In re Wilka, 12 A. B. R. 728 (D. C. Iowa): "The referee finds, however, that the trustee was in the actual possession of the property. If this is true, though the property may then have been situated in South Dakota, the court was in the actual custody and possession of the property through its trustee. * * * In this case the Granite City Bank was given the notice required by the Bankruptcy Act and by personal service of such notice upon it at Dell Rapids, S. D., as well. The conclusion is that the referee had jurisdiction to make the order of sale. This, of course, does not preclude the bank from establishing its claim, if it can do so, to the proceeds of the property covered by its mortgage. It may propound its claim thereto before the referee. In fact, the referee should require it to do so before making any order for the distribution of such proceeds. Upon the bank's presenting its claim to such proceeds, the trustee may take issue thereon, if he so elects, and the referee will then determine the matter upon evidence taken under his direction."

In re Miner's Brewing Co., 20 A. B. R. 717, 162 Fed. 327 (D. C. Pa.): "Under the facts reported by him, the referee had authority to order a sale of the bankrupt's real estate discharged of liens. Upon these facts, he had authority also to hear claims upon the fund produced by the sale, and to determine their validity, extent and relative priority."

B. R. 807, 172 Fed. 535 (C. C. A. N. Y.): "Doubtless a court of equity would not intervene to enforce or perfect an imperfect mortgage as against the other creditors of the mortgagor."

42. Impliedly, Mound Mines Co. v. Hawthorne, 23 A. B. R. 242, 173 Fed. 882 (C. C. A. Colo.).

43. In re Granite City Bk., 14 A. B. R. 404, 137 Fed. 818 (C. C. A. Iowa, affirming In re Wilka, 12 A. B. R. 727, 131 Fed. 1004); In re Sanborn, 3 A. B. R. 54, 96 Fed. 507 (D. C. Vt.); In re Kellogg, 10 A. B. R. 7, 121 Fed. 333 (C. C. A. N. Y.); impliedly, In re Keller, 6 A. B. R. 351 (D. C. Iowa); In re McBride & Co., 12 A. B. R. 83, 132 Fed. 285 (Ref. N. Y.); In re

Steuer, 5 A. B. R. 209, 104 Fed. 976 (D. C. Mass.); In re Moody, 12 A. B. R. 725, 131 Fed. 525 (D. C. Iowa); In re Bacon, 12 A. B. R. 730, 132 Fed. 157 (D. C. N. Y.); In re Pollman, 16 A. B. R. 144 (Ref. N. Y.); Instance, Smith v. Township, 17 A. B. R. 747 (C. C. A. N. J.); In re Pittelkow, 1 A. B. R. 472, 92 Fed. 901 (D. C. Wis.); In re Matthews, 6 A. B. R. 96, 109 Fed. 603 (D. C. Ark., affirmed in Chauncey v. Dyke Bros., 9 A. B. R. 444, 119 Fed. 1, C. C. A. Ark.); In re Schrinopskie, 10 A. B. R. 221 (D. C. Kans.); Instance, In re Kohl-Hepp Brick Co., 23 A. B. R. 822, 176 Fed. 340 (C. C. A. N. Y.), quoted, on other points, at §§ 1970, 1979, 1980.

Even where the transfer complained of occurred more than four months preceding the bankruptcy.

In *re Elletson Co.*, 23 A. B. R. 530, 174 Fed. 859 (D. C. W. Va.): "This deed having been executed more than four months prior to the institution of bankruptcy proceedings, under older decisions some doubt might have arisen as to the right of the referee to pass upon and adjudicate the matter in this summary proceeding instead of requiring the institution of a plenary suit for the purpose. The bank, however, having voluntarily submitted to the jurisdiction by presenting its claim for adjudication, and the estate of the bankrupt being wholly in the possession of the court, there can no longer be doubt of the jurisdiction as thus taken by the referee under the rulings. Indeed the question of 'four months' or not has nothing to do with the jurisdiction of the referee, that jurisdiction being dependent rather on possession of the res."

Whilst it is true that the referee has such jurisdiction, and that generally such proceedings should be had before the referee, and perhaps, under rule of court would be sent there if filed in the District Court, yet this is not to deny that the District Court, before the judge itself, has jurisdiction to entertain the proceedings if it so desires. However, after reference to the referee all proceedings relative to property in the custody of the court should, for the sake of due order and consistent administration, be carried on before the referee; and such is the evident design of the Act.

§ 1889. Reasonable Notice to Lienors or Other Parties in Interest Requisite.—Notice must be given to lienholders;⁴⁴ and a sale does not divest the lien of a creditor unless he has been given such notice and unless the sale has been made free therefrom.⁴⁵

Reasonable notice to the various lienholders and claimants of interest, to come in and set up their rights, is all that is requisite.⁴⁶

44. In *re Foundry & Machine Co.*, 17 A. B. R. 293, 147 Fed. 828 (D. C. Wis.); In *re Kohl-Hepp Brick Co.*, 23 A. B. R. 822 (C. C. A. N. Y.), quoted at § 1980; In *re Sanborn*, 3 A. B. R. 54, 96 Fed. 551 (D. C. Vt.); In *re Saxton Furnace Co.*, 14 A. B. R. 483, 136 Fed. 697 (D. C. Pa.); *Mound Mines Co. v. Hawthorne*, 23 A. B. R. 242, 173 Fed. 882 (C. C. A. Colo.), quoted at § 1888; *obiter*, In *re Gerdes*, 4 A. B. R. 447, 102 Fed. 318 (D. C. Ala.). See post, § 1980.

45. See post, § 1980; In *re Kohl-Hepp Brick Co.*, 23 A. B. R. 822, 176 Fed. 340 (C. C. A. N. Y.), quoted at § 1980; *Bassett v. Thacker*, 16 A. B. R. 787, 72 N. J. L. 81, 60 Atl. 39; In *re Foundry Machine Co.*, 17 A. B. R. 293, 147 Fed. 828 (D. C. Wis.).

46. In *re Rochford*, 10 A. B. R. 608, 124 Fed. 182 (C. C. A. S. Dak.); In *re Granite City Bank*, 14 A. B. R. 404, 409, 137 Fed. 818 (C. C. A. Iowa, affirming In *re Wilka*, 12 A. B. R. 727, 131 Fed. 1004), which was a case of

giving notice to lienors living out of the jurisdiction holding liens on personal property. In *re Kellogg*, 10 A. B. R. 7, 121 Fed. 333 (C. C. A. N. Y.). Impliedly, In *re McBride & Co.*, 12 A. B. R. 83, 132 Fed. 285 (Ref. N. Y.).

Compare, In *re Waukesha Water Co.*, 8 A. B. R. 715, 116 Fed. 1009 (D. C. Wis.), as to notice on persons in another district (in cases, however, where such persons are in possession of the instrument sought to be canceled).

In *re Pittelkow*, 1 A. B. R. 472, 92 Fed. 901 (D. C. Wis.).

In *re Scrinopskie*, 10 A. B. R. 221 (D. C. Kans.), where the referee held a sale of property to have been fraudulent as to creditors although conveyance made more than four months before bankruptcy.

In *re Wilka*, 12 A. B. R. 729, 131 Fed. 1004 (D. C. Iowa, affirmed sub nom. in In *re Granite City Bk.*, 14 A. B. R. 404, 137 Fed. 818); *obiter*, In *re Gerdes*, 4 A. B. R. 347, 102 Fed.

United Sheet & Tin Plate Co. v. Hess, 20 A. B. R. 254, 159 Fed. 889 (C. C. A. Ohio): "There is no better established principle than that all parties interested, whose rights will be directly affected by the decree, must be made parties to the suit. * * * The relief which the petitioners sought was directly hostile to the mortgage of September 1, 1893."

In re Moody, 12 A. B. R. 724, 131 Fed. 525 (D. C. Iowa): "It is a familiar principle of equity jurisprudence that property in the custody of a court of equity is always held by it in trust for those to whom it rightly belongs; and the jurisdiction to inquire into and determine to whom it so belongs, and to that end to receive all claimants thereto to present their claims within a stated time, or be barred of any interest in or right to the property, is inherent in every court of equity. In re Rochford (C. C.), 10 A. B. R. 608, 124 Fed. 187, above. And this though the property may have been wrongfully seized, and so brought into the custody of the court. Krippendorf v. Hyde, 110 U. S. 276. See, also, Freeman v. Howe, 24 How. 450, and Buck v. Colbath, 3 Wall. 334; Bryan v. Bernheimer, and In re Rochford, above, establish the rule by which the right to this stock of merchandise or its proceeds so in the custody of the court may be fully determined; and that is to require the land company to propound its claims to such property to the bankruptcy court within a stated time. The motion of the Hawkeye Land Company for the release of the property will therefore be overruled, and it will be required to propound its claim to this property before the referee by September 1, 1904. The referee will so notify it at least 10 days before such date, and, if it fails to do so within such time, it will be barred of all right to or interest in said property. If it shall so propound its claim, the referee will then fix the time within which the trustee, as soon as appointed, shall plead thereto, and will make all requisite and necessary orders for speeding the matter to a final hearing, and determine the questions so presented."

In re Noel, 14 A. B. R. 720, 137 Fed. 694 (D. C. Md.): "That court, having possession of the property, had jurisdiction, upon notice to those claiming to have liens and incumbrances upon it, to order the property to be sold by the trustees free of all incumbrances, if the court, in its discretion, should determine that such a sale was for the benefit of the unsecured creditors; and after such a sale, having in its control the fund arising from the sale, it would have jurisdiction to determine the conflicting claims of the parties whose liens had been displaced as to the property sold, and transferred to the fund in the court. Ray v. Norseworthy, 23 Wall. 128, 23 L. Ed. 116."

Even when a lienor on property in the actual custody of the bankruptcy court is also a creditor, he must have due notice, other than the mere ten days notice by mail given to all creditors, of any attempt to affect his property rights as such lienor.⁴⁷ Even though the claim be considered frivo-

318 (D. C. Ala.); In re Sanborn, 3 A. B. R. 54, 96 Fed. 551 (D. C. Vt.); In re Saxton Furnace Co., 14 A. B. R. 483, 136 Fed. 697 (D. C. Pa.); Mound Mines Co. v. Hawthorne, 23 A. B. R. 242, 173 Fed. 882 (C. C. A. Colo.), quoted at § 1888; In re Foundry & Machine Co., 17 A. B. R. 293, 147 Fed. 828 (D. C. Wis.). See post, § 1980.

Not to Adjudicate Lien in Favor of Lienholder Not a Party When.—Nor should the order require payment of a lien to a lienholder not made a party nor appearing in the proceed-

ings, unless the pleadings already filed therein expressly concede the validity and extent of the lien and the person entitled thereto. Gillespie v. Piles, 24 A. B. R. 502, 178 Fed. 886 (C. C. A. Iowa), quoted at § 562.

⁴⁷. But see, apparently, contra, In re Wilka, 12 A. B. R. 727, 131 Fed. 1004 (D. C. Iowa). However, on review (sub nom. In re Granite City Bk., 14 A. B. R. 405 [C. C. A. Iowa]) it is evident that actual notice was given to lienors.

lous, the alleged lienor should be given notice.⁴⁸ However, the failure to give him notice would not make the sale invalid, but would simply make it subject to whatever rights the alleged lienor might be able to prove.

Likewise notice must be given to adverse claimants, where any disposition of the property in which they claim to be interested is concerned.⁴⁹ Thus, the court held a trustee in bankruptcy personally liable to an adverse claimant where the trustee turned the property back to the bankrupt upon confirmation of a composition, after having actual notice of the adverse claimant's rights.⁵⁰

§ 1890. "Ten Days Notice by Mail" Insufficient; "Order to Show Cause," Proper Method.—The usual ten days notice by mail prescribed in cases of sales, etc., will not suffice. Ordinarily, notice is given by means of the service of a certified copy of an "order to show cause" by a certain date why the prayer of the petition should not be granted.⁵¹ Of course, the parties may waive service of process and enter their appearance voluntarily.⁵²

There is no need to give notice, however, of the application for an order to show cause—the show-cause order is itself a notice to appear and it concludes no one.

In *re Philip Brady*, 21 A. B. R. 364, 169 Fed. 152 (D. C. Ky.): "While a notice might not have been improper, it was not at all necessary, because the show-cause order itself gives notice and affords an opportunity on a certain named future day to show cause why the special relief sought should not be granted. The order, per se, gives him his day in court."

Similarly, an "order to show cause" may be issued upon the trustee upon a claimant's petition or cross petition, where notice upon the trustee is proper.⁵³

§ 1891. Notice on Nonresidents, if Court Has Actual Possession.—Where the bankruptcy court has actual possession of the property involved, notice may be served upon parties out of the district to set up their rights.⁵⁴ Service may be had on nonresidents under U. S. Rev. Stat., § 738.⁵⁵

48. In *re Kohl-Hepp Brick Co.*, 23 A. B. R. 822, 176 Fed. 340 (C. C. A. N. Y.).

49. Apparently notice not requisite upon beneficiary in life insurance policy, where policy provides for change of beneficiary, before ordering bankrupt to apply for change of beneficiary to trustee. In *re Orear*, 24 A. B. R. 343, 178 Fed. 632 (C. C. A. Mo.). However, since the decision in *Burlingham v. Crouse*, 30 A. B. R. 8, 228 U. S. 459, the case In *re Orear* is not authority so far as concerns life insurance policies as assets.

50. In *re Cadenas & Coe*, 24 A. B. R. 135, 178 Fed. 158 (D. C. N. Y.).

51. See post, "Selling Property Subject to and Free from Liens," § 1981.

52. *Kurtz v. Young*, 12 A. B. R. 509, 131 Fed. 719 (C. C. A. Minn.). And see ante, § 1838.

53. Instance, In *re MacDougall*, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.).

54. In *re Wilka*, 12 A. B. R. 727, 131 Fed. 1004 (D. C. Iowa), affirmed in *re Granite City Bank*, 14 A. B. R. 404, 137 Fed. 818 (C. C. A.). Inferentially, *Horskins v. Sanderson*, 13 A. B. R. 101 (D. C. Vt.). Obiter [rule conceded but held inapplicable to summary orders], *Staunton v. Wooden*, 24 A. B. R. 736, 179 Fed. 61 (C. C. A. Cal.), quoted at § 1705½.

55. Inferentially, *Horskins v. Sanderson*, 13 A. B. R. 101, 132 Fed. 415 (D. C. Vt.).

§ 1892. **But Mere Possession of Res and Service of Notice Insufficient to Render Judgment in Personam.**—While possession of the property involved entitles the bankruptcy court in such summary proceedings to determine the rights of the parties thereto and to adjudicate those rights upon proper notice, yet, if there be no waiver of jurisdiction and no entry of appearance, the mere possession of the rem and service of notice on the party will not authorize the bankruptcy court to render personal judgment for costs against such third party.⁵⁶

§ 1893. **Third Parties May Intervene.**—On the other hand third parties claiming interests in the property may intervene and apply to be made parties, set up their rights and have them determined in the bankruptcy court.

In re Goldsmith, 9 A. B. R. 426, 118 Fed. 763 (D. C. Tex.): "I. Hirsch & Son come as intervenors seeking to subject certain funds, which arose from the sale of the property on which they claim a lien, to the part payment of an alleged indebtedness. They have a right to come in this way. *Fisher v. Cushman*, 4 A. B. R. 646, 103 Fed. 860; In re Oconee Mill Co., 6 A. B. R. 475, 109 Fed. 866."

§ 1894. **Pleadings and Practice in Marshaling Liens and Interests.**—Liens may be set up on the forms prescribed by the Supreme Court's General Orders in Bankruptcy for proof of secured debts.⁵⁷ But secured creditors are not obliged to prove their claims upon the form prescribed by the Supreme Court for proof of secured debts. A mere pleading in the nature of an intervening petition in equity will suffice, the regular form apparently being intended simply for secured creditors who retain the possession of their securities and desire their value credited thereon and the claim allowed for the deficit.⁵⁸

56. *Havens & Geddes Co. v. Pierek*, 9 A. B. R. 569, 120 Fed. 244 (C. C. A. Ills.); Although this case states the rule in the broad form that the bankruptcy court has no jurisdiction at all to maintain a plenary action, as was the case before the amendment of 1903 conferred such jurisdiction, yet on the proposition of the text, it still states the true rule where the proceedings are not a plenary suit but the usual proceedings to marshal liens, etc., before the referee.

57. Inferentially, *Burow v. Grand Lodge*, 13 A. B. R. 545, 133 Fed. 542 (C. C. A. Tex.). See post, § 1985.

58. In re Goldsmith, 9 A. B. R. 419, 118 Fed. 763 (D. C. Tex.); *Burow v. Grand Lodge*, 13 A. B. R. 545, 133 Fed. 542 (C. C. A. Tex.); *Carriage Co. v. Solanas*, 6 A. B. R. 225 (D. C. La.); impliedly, In re Bellevue Pipe & F'dy Co., 22 A. B. R. 97, 16 Ohio Dec. 247 (Ref. Ohio); In re Stevens, 23 A. B. R. 239, 113 Fed. 842 (D. C. Ore.),

quoted at § 758½. The subject of pleadings and practice in proceedings to marshal liens is taken up fully under the subject of "Selling Property Free from Liens," post, § 1965.

Whether the petition must expressly allege possession to be in trustee, In re Granite City Bk., 14 A. B. R. 408, 137 Fed. 818 (C. C. A. Iowa).

As to rules regarding the reopening of the case for further testimony, see § 553½; compare rules regarding objections to claims, etc., § 830, et seq.

Necessary Allegations to Set Aside Fraudulent and Preferential Transfers.—For necessary allegations on the part of the trustee to avoid preferential or fraudulent transfers, compare analogous rules, ante, § 1731.

Whether Trustee to Show Inadequacy of Assets.—See ante, § 1731. Compare, In re Standard Tel. & Elec. Co. (*Knapp v. Milw. Tr. Co.*), 24 A. B. R. 761, 216 U. S. 545, quoted at § 1731, to the effect that it is no de-

The hearing should not be upon affidavits, for the proceedings are not in the nature of a mere motion but rather of a petition.⁵⁹

§ 1894¹/₂. Statutory Regulations of Right to Institute or Maintain Suit Not Applicable.—State regulations of the right of a party to institute or maintain suit are not applicable to proceedings in the bankruptcy court.

In re Farmers Supply Co., 22 A. B. R. 460, 170 Fed. 502 (D. C. Ohio): "The jurisdiction and remedies conferred by the Constitution and statutes of the United States on the national courts are uniform throughout the different states of the Union, and cannot be impaired, restricted, or destroyed by state legislation, which prescribes a condition only by compliance with which a partnership having a fictitious name may commence and maintain litigation in its own courts."

§ 1895. Whether Proceedings to Marshal Liens on Property in Custody, on Notice, Strictly "Summary" Proceedings.—Proceedings to marshal liens on property in the custody of the bankruptcy court, on notice and hearing, perhaps are not, strictly speaking, "summary" proceedings even though they do not follow the established forms.⁶¹

§ 1896. What Law Governs Validity.—In general the trustee takes title in the same plight and condition in which the bankrupt left it. In general the law of the State will control in the marshaling of liens; and the decisions of the highest tribunal of the State will be followed where the lien or interest is not affected by the peculiar provisions of the Bankruptcy Act. In short, the validity and priority of liens on the property so coming into the custody of the bankruptcy court, and the extent and validity of interests therein are, in general, to be determined by the law of the State.⁶²

fense to a charge that the transfer is preferential or fraudulent to show that the trustee might possibly recover enough from unpaid stock subscriptions and by suit against officers and directors, to pay all debts.

59. Analogously, In re Bailey, 19 A. B. R. 470, 156 Fed. 691 (D. C. N. Y.).

61. In re McMahon, 17 A. B. R. 534, 147 Fed. 685 (C. C. A. Ohio). Also, see ante, "What Is Summary Process," § 1832.

62. See the various discussions as to the title of the trustee, the same necessarily involving the law applicable to the marshaling of liens in bankruptcy. Thompson v. Fairbanks, 13 A. B. R. 437, 196 U. S. 516; Humphrey v. Tatman, 14 A. B. R. 74, 198 U. S. 91; York Mfg. Co. v. Cassell, 15 A. B. R. 633, 201 U. S. 342; First Nat'l Bk. v. Staake, 15 A. B. R. 639, 202 U. S. 141; In re Josephson, 8 A. B. R. 423, 116 Fed. 404 (D. C. Ga.); as to unrecorded chattel mortgage, Deland v.

Miller, 11 A. B. R. 744, 119 Iowa 368; Morgan v. Nat'l Bk., 16 A. B. R. 644, 145 Fed. 466 (C. C. A. W. Va.); Analogously (a pledge in pledgee's hands). In re Byrne, 3 A. B. R. 268, 97 Fed. 762 (D. C. Iowa); In re Forbes, 7 A. B. R. 42 (Ref. Ohio): Dower computed on equity of redemption where purchase money mortgage exists, in Ohio, In re Hawkins, 9 A. B. R. 598 (D. C. R. I.): Dower, in Rhode Island, computed on whole value, but payable out of equity of redemption. In re Waterloo Organ Co., 9 A. B. R. 429, 118 Fed. 904 (D. C. N. Y.); Bush v. Export Storage Co., 14 A. B. R. 138, 136 Fed. 918 (U. S. C. C. Tenn. on page 168, interpreting Thompson v. Fairbanks, 13 A. B. R. 437, 196 U. S. 516).

In re Lukens, 14 A. B. R. 683, 133 Fed. 188 (D. C. Penn.), where a real estate mortgage not recorded until after adjudication of mortgagor and appointment of trustee was held void

Hiscock v. Varick Bk., 206 U. S. 28, 18 A. B. R. 6: "The contracts of pledge were made, executed and to be performed in the State of New York, and the rights of the parties were governed by the law of that State. No preference under the Bankruptcy Act was alleged or proved, nor was there any allegation or proof that the pledge of the securities was in fraud of the rights of the creditors or trustee. The questions of the extent and validity of the pledge were local questions, and the decisions of the courts of New York are to be followed by this court."

In re *National Bk.*, 14 A. B. R. 180, 135 Fed. 62 (C. C. A. Ohio): "In determining the validity of a chattel mortgage, this court will endeavor to follow the settled law of the State in which the transaction occurred."

Instance, In re *Bailey*, 24 A. B. R. 201, 176 Fed. 990 (D. C. Utah); creditor holding lien on exempt and non-exempt property, not obliged to exhaust lien on exempt property first, the fact of its being exempt being held to vary the rule.

In re *Elletson Co.*, 23 A. B. R. 530, 174 Fed. 859 (D. C. W. Va.): "The Supreme Court has determined that the question whether such a deed of trust is valid or not is a local one and must be governed by the State court decisions, which the Federal courts will follow."

§ 1897. Where Rights under State Statute Dependent on Resort to Special Remedies.—But where the state law confers certain rights upon creditors to set aside conveyances, wholly dependent, however, upon their institution of litigation in certain form in the state courts, the funds in the hands of the bankruptcy court probably will not be adminis-

under § 67 (a). However, unless the Pennsylvania law declares a real estate mortgage void as to creditors for nonrecording, it is hard to see how it would be void as to the trustee in bankruptcy who simply represents creditors.

Instance, In re *Gosch*, 9 A. B. R. 613, 121 Fed. 604 (D. C. Ga.), wherein it was held that a sash and door factory was not a "saw mill" within the meaning of the Georgia Lien Law.

Instances, *Chauncey v. Dyke Bros.*, 9 A. B. R. 444, 119 Fed. 1 (C. C. A. Ark.), wherein the statute of Arkansas was applied, giving priority to mechanics' liens over a prior mortgage, except in so far as the prior mortgage is made to raise money to make the improvements and the improvements are actually made.

Instance, *Ludowici Roofing Tile Co. v. Penn. Inst.*, 8 A. B. R. 739 (D. C. Penn.): Building contract stipulating against liens recorded, bars subcontractors, in Pennsylvania, notwithstanding further stipulations that final payment need not be made unless receipts in full from lienholders be exhibited—later stipulation being for owner's benefit.

Instance, *Cunningham v. Germ. Ins.*

Bk., 4 A. B. R. 363 (C. C. A. Ky.): Validity of mortgage where loan in excess of charter.

Instance, *Ludowici Roofing Tile Co. v. Penn. Inst.*, 8 A. B. R. 739 (D. C. Penn.): Partial assignments of building contract fund where fund turned over to the bankruptcy court for marshaling of liens, will be honored.

Instance, In re *Byrne*, 3 A. B. R. 268, 97 Fed. 762 (D. C. Iowa): Statute of Iowa giving wages of employees priority over existing mortgage.

Instance, *Morgan v. Nat'l Bk.*, 16 A. B. R. 639, 145 Fed. 466 (C. C. A. W. Va.): Priorities in W. Va. between mechanics' liens and bonded indebtedness of a manufacturing plant.

Instance, In re *Dunavant*, 3 A. B. R. 41, 96 Fed. 542 (D. C. N. Car.): Statute of Limitations as to alleged fraudulent transfers.

Instance, In re *Cannon*, 10 A. B. R. 64, 121 Fed. 582 (D. C. S. C.): Unrecorded chattel mortgage void by State law only as to subsequent creditors; fund will be divided first among subsequent creditors.

First Nat. Bk. v. *Guarantee Title & Trust Co.*, 24 A. B. R. 330, 178 Fed. 187 (C. C. A. Pa.), quoted at § 1140. See ante, §§ 780, 1140.

tered nor distributed in accordance therewith,⁶³ even where such suit is already pending at the time of bankruptcy; especially where actual custody and possession of the property has not been taken by the state court but has been taken by the bankruptcy court; and especially where the state court proceedings would have resulted in "class" preference.⁶⁴

Likewise, where the statute requires conditional vendors to refund part of the purchase price on taking possession, such refund will not be required where the conditional vendor does not petition for surrender of the property, but merely for a marshaling of the liens and payment of the balance of his purchase price as an equitable lien.⁶⁵

§ 1898. Rights of Priority under State Statutes as Related to Marshaling of Liens on Property.—Where, by state law, the putting of property into the hands of a receiver or assignee operates to give a right of priority to operatives for labor performed by them during a certain period preceding the receivership or assignment, then, in such cases, upon the subsequent bankruptcy of the debtor and the transfer of the property to the bankruptcy court for administration, the special provisions of the Bankruptcy Act giving priority to wages earned by the similar classes of "workmen, clerks and servants," supersedes the order of priority of the state statute and the claims must be made under this provision of the Bankruptcy Act and not under the state law; but as to other priorities, if the state statute confers them as general rights of priority, they will have the same priority, in the marshaling of liens in bankruptcy that they would have had in the marshaling of liens in the state court.⁶⁶ But in no event will workmen, clerks nor servants, under the Bankruptcy Act (nor as a general rule, operatives under the state laws) have priority of payment of their wages out of the proceeds of property over a mortgage or other contract lien thereon made upon a presently passing consideration and duly recorded.⁶⁷ But such right of priority under state law given to employees

63. For full discussion, see ante, § 1266, et seq.

64. In re Porterfield, 15 A. B. R. 17, 138 Fed. 192 (D. C. W. Va., reversed sub nom. *Moore v. Green*): "I hold that the petitioning creditors, independent of the exclusive character of the bankruptcy jurisdiction, cannot now rely upon the pendency of the case in the State court to give them the relief asked, to-wit, the distribution of the funds according to the requirements of § 2, c. 74, of the Code of West Virginia of 1899; and this for two reasons: (a) Because the State court never took possession of the property; and (b) because the parties have, in effect waived any rights they might have had in this particular, and have submitted to the federal court's jurisdiction."

65. See ante, § 1878; also, see In re

Max Goldman, 23 A. B. R. 497, 174 Fed. 579 (C. C. A. Ohio), quoted at § 1878.

66. See post, § 2202, et seq.

67. In re Meis, 18 A. B. R. 107 (Ref. Ky.); In re Frick, 1 A. B. R. 719 (Ref. Ohio).

Compare, analogously, contra, In re Duncan, 2 A. B. R. 321 (D. C. Tex.): But this probably was a case of a landlord's right of mere priority rather than of a specific lien.

Contra, obiter, under laws of Iowa, In re Byrne, 3 A. B. R. 268, 97 Fed. 762 (D. C. Iowa). Contra, In re Tebo, 4 A. B. R. 235, 101 Fed. 235 (D. C. W. Va.). Also, see post, § 2206, et seq. At any rate, where the wages claimed upon were not even earned when the mortgage was given. In re Mulhauser Co., 10 A. B. R. 231, 121 Fed. 669 (C. C. A. Ohio).

may take precedence over certain statutory liens, such as landlords' liens; ⁶⁸ and, in some states, over mortgages given on a "plant" or business.⁶⁹

§ 1899. "Surrender of Preference" on Distinct Transaction Not to Be Required as Prerequisite to Validity of Lien Which Itself Is Not a Preference.—Surrender of preferences received on other and distinct transactions is not to be required upon the marshaling of assets, as a condition prerequisite to the validity of a lien, where the lien itself is not a preference. Such surrender is a prerequisite only to the allowance of claims to share in dividends.⁷⁰

DIVISION 6.

SUMMARY JURISDICTION OVER TRUSTEE AND RECEIVER TO PREVENT THEIR INTERFERENCE WITH RIGHTFUL POSSESSION OF THIRD PARTIES.

§ 1900. Summary Jurisdiction to Prevent Trustee Interfering with Others' Rightful Custody.—The bankruptcy court has summary jurisdiction over its own receiver, trustee or other officer to control his actions towards third parties and to prevent his interference with their lawful custody.⁷¹

DIVISION 7.

RESTRAINING ORDERS AND INJUNCTIONS IN AID OF BANKRUPTCY PROCEEDINGS.

§ 1901. Jurisdiction to Issue Injunctions in Aid of Bankruptcy Proceedings.—Restraining orders may be issued by the bankruptcy court in the bankruptcy proceedings themselves, in aid of the collection of the assets and their reduction to money, prohibiting third parties from interfering with the property or its custody, or from taking other action in relation thereto.⁷²

^{68.} See post, § 2202.

^{69.} See post, § 2202, et seq.

^{70.} In re Franklin, 18 A. B. R. 218, 151 Fed. 642 (D. C. N. Car.).

^{71.} In re Tomlinson, 27 A. B. R. 780, 193 Fed. 101 (D. C. N. Y.). Compare, Warehousing Co. v. Hand, 16 A. B. R. 56 (C. C. A. Wis.), where the bankruptcy court entertained a plenary intervening petition to enjoin the trustee from interfering with the petitioner's possession.

Contra, In re Berkowitz, 16 A. B. R. 255, 143 Fed. 598 (D. C. Penn.), where the bankruptcy referee attempted to restrain the trustee from replevying property from the bankrupt's wife, the reviewing court reversing the referee. Compare, In re Howard, 12 A. B. R. 462 (D. C. Calif.).

"Order to show cause" upon trustee.

Instance, In re MacDougall, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.).

^{72.} Compare, ante, "Provisional Remedies and Restraining Orders before the Appointment of Trustees," § 359. Also various subjects wherein injunction has been sought as a remedy.

Compare, "Injunctions and Restraining Orders on Plenary Actions Brought by Trustees and Receivers," ante, § 1727.

Compare, as to law of 1867, cases cited in note to Keegan v. King, 3 A. B. R. 79.

In re Goldberg, 9 A. B. R. 156, 117 Fed. 692 (D. C. N. Y.), quoted, ante, § 359; In re Hornstein, 10 A. B. R. 308, 122 Fed. 266 (D. C. N. Y.), quoted, ante, § 359; In re Breslauer, 10 A. B. R. 33, 121 Fed. 910 (D. C. N. Y.); In re Kenney, 2 A. B. R. 494, 95 Fed. 427

Bear v. Chase, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S. C.): "Counsel insist with great earnestness that a bill in equity should have been filed in this case instead of proceeding by rule to show cause, as was done, and while it is not said so in words, the inference is irresistible that it was necessary to institute such suit in the State Court instead of the District Court of the United States. * * * It may be conceded that in ordinary proceedings affecting the bankrupt's estate, in which third parties or adverse claimants are interested, the better practice would be either to file a bill in equity or a separate petition in the bankruptcy proceedings, setting up the cause of action in question, on which process should be regularly issued or full opportunity otherwise given to appear. But that has no application in this case, where the alleged ground of bankruptcy is the procuring of and levying the attachments enjoined. * * * Upon the adjudication of the bankrupt, all creditors became parties to the bankruptcy proceedings by operation of law, and particularly these creditors

(D. C. N. Y., affirmed in 3 A. B. R. 353 and 5 A. B. R. 355, and reaffirmed sub nom. *Clarke v. Larremore*, 9 A. B. R. 476, 188 U. S. 486); *Lesser Bros.*, 5 A. B. R. 320 (C. C. A. N. Y., reversed, on other grounds, sub nom. *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165); *Blake v. Francis-Valentine Co.*, 1 A. B. R. 372 (D. C. Calif.): This case, however, is not to be approved to its full extent.

In *re Northrop*, 1 A. B. R. 427 (Ref. N. Y.); In *re Globe Cycle Wks.*, 2 A. B. R. 447 (Ref. N. Y.); In *re Chas. D. Adams*, 1 A. B. R. 94 (Ref. N. Y.); In *re Lemmon & Gale Co.*, 7 A. B. R. 291, 112 Fed. 296 (C. C. A. Tenn.); In *re Whitener*, 5 A. B. R. 198, 105 Fed. 180 (C. C. A. N. Y.); In *re Ball*, 9 A. B. R. 276, 118 Fed. 672 (D. C. Vt.), quoted, ante, § 359. In *re Kerski*, 2 A. B. R. 79 (Ref. Wis.): This case, however, states the rule too broadly. In *re Smith*, 8 A. B. R. 55, 113 Fed. 993 (D. C. Ga.), quoted, ante, § 359. In *re Tiffany*, 13 A. B. R. 310, 133 Fed. 799 (D. C. N. Y.); In *re Miller*, 9 A. B. R. 274, 118 Fed. 360 (D. C. Ga.); In *re Jersey Island Packing Co.*, 14 A. B. R. 689, 138 Fed. 625 (C. C. A. Calif.); In *re Eastern Commission & Importing Co.*, 12 A. B. R. 305, 129 Fed. 847 (D. C. Mass.); In *re Tune*, 8 A. B. R. 285, 115 Fed. 906 (D. C. Ala.); In *re Huddleston*, 1 A. B. R. 572 (Ref. Ala.); In *re Mertens*, 12 A. B. R. 698, 131 Fed. 507 (D. C. N. Y.); In *re Booth*, 2 A. B. R. 770, 96 Fed. 943 (D. C. Ga.); In *re Jackson*, 2 A. B. R. 501, 94 Fed. 797 (D. C. Vt.); In *re Adams*, 14 A. B. R. 23, 134 Fed. 142 (D. C. Conn.); In *re Vastbinder*, 13 A. B. R. 148, 132 Fed. 718 (D. C. Penn.); In *re Baughman*, 15 A. B. R. 23, 138 Fed. 742 (D. C. Penn.); In *re Klein*, 3 A. B. R. 174, 97 Fed. 31 (D. C. Ills.); In *re Currier*, 5 A. B. R. 639 (Ref. N. Y.); obiter, *Carling v. Seymour Lumber Co.*, 8

A. B. R. 41, 113 Fed. 483 (C. C. A. Ga.); In *re Riker*, 5 A. B. R. 720, 107 Fed. 96 (C. C. A. N. Y.); *Bindseil v. Smith*, 5 A. B. R. 40 (Court of Errors N. J.); In *re Steuer*, 5 A. B. R. 209, 104 Fed. 976, 980 (D. C. Mass.); *Beach v. Macon Grocery Co.*, 8 A. B. R. 752, 116 Fed. 143 (C. C. A. Ga.); In *re Krinsky Bros.*, 7 A. B. R. 535, 112 Fed. 972 (D. C. N. Y.), quoted, ante, § 359. In *re Weinger, Bergman & Co.*, 11 A. B. R. 424, 126 Fed. 875 (D. C. N. Y.); *White v. Schloerb*, 4 A. B. R. 178, 178 U. S. 542.

Instances, *O'Dell v. Boyden*, 17 A. B. R. 755, 150 Fed. 731 (C. C. A. Ohio.); In *re Kleinhans*, 7 A. B. R. 604, 113 Fed. 107 (D. C. N. Y.); In *re Barrett*, 12 A. B. R. 626, 132 Fed. 362 (D. C. Tenn.); In *re Wilkes*, 7 A. B. R. 574, 112 Fed. 975 (D. C. Ark.); In *re Martin*, 5 A. B. R. 423, 105 Fed. 753 (D. C. N. Y.).

Compare, as to jurisdiction to stay suits to permit the bankrupt to interpose discharge, post, § 2696, et seq.; In *re Dana*, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.), quoted at § 1796. *Berman v. Smith*, 22 A. B. R. 662, 171 Fed. 735 (D. C. Ga.); In *re Bluestone Bros.*, 23 A. B. R. 264, 174 Fed. 53 (D. C. W. Va.), quoted at § 1908.

Instance (restraining landlord), In *re Schwartzman*, 21 A. B. R. 885, 167 Fed. 399 (D. C. S. C.), quoted at § 984.

In *re Roger Brown & Co.*, 28 A. B. R. 336, 196 Fed. 758 (C. C. A. Iowa); In *re Swofford Bros. Dry Goods Co.*, 25 A. B. R. 282, 180 Fed. 549 (D. C. Mo.).

Action brought to compel accounting for an inequitable advantage obtained by an officer of a bankrupt corporation over its stockholders. In *re Swofford Bros. Dry Goods Co.*, 25 A. B. R. 282, 180 Fed. 549 (D. C. Mo.).

by whose acts the bankruptcy was caused. No good reason would seem to exist why a court, as to any creditor before it in a bankruptcy proceeding, should not, after the service of a rule, enjoin such creditor from taking any step or doing any act affecting the bankrupt's estate, or interrupting the court in the due administration thereof. These attaching creditors do not occupy the relation of third persons in possession of, or adverse claimants dealing with, the property of the bankrupt. In *re Kennedy* (D. C.), 97 Fed. (3 Am. B. R. 353) 557, 558. They are but creditors of the bankrupt, who have, in their effort to collect their money, sought an advantage which the law does not give, and they cannot gain any favored position by reason of an act of theirs which the law condemns."

New River Coal Land Co. v. Ruffner, 20 A. B. R. 100, 165 Fed. 881 (C. C. A. W. Va.): "We have given careful consideration to the arguments submitted and are of opinion that the order granting a stay of proceedings in the State court was clearly authorized by the Bankruptcy Act. In the administration of the affairs of insolvent persons and corporations the jurisdiction of the federal courts in bankruptcy is essentially exclusive. 'The intent of the bankruptcy law,' says the Supreme Court in *re Watts and Sachs*, 190 U. S. 27, 10 Am. B. R. 113, 'is to place the administration of affairs of insolvents exclusively under the jurisdiction of the bankruptcy courts.'"

In *re Russell & Birkett*, 3 A. B. R. 658, 101 Fed. 248 (C. C. A. N. Y.): "A Federal court will neither interfere with property in the lawful custody of a State court, nor tolerate interference by a State court with property in its custody. * * * Authority to Courts of Bankruptcy to protect the property in their custody from such interference would seem to be specifically conferred by that provision of § 2 of the act permitting them to make such orders and issue such processes as may be necessary for enforcing their jurisdiction. The prohibition of § 720 of the Revised Statutes against enjoining the proceedings of a State court does not apply when any law relating to bankruptcy authorizes an injunction, nor does it where the proceedings sought to be enjoined have been commenced after the jurisdiction of the Federal court has attached."

In *re Emslie*, 4 A. B. R. 126, 102 Fed. 292 (C. C. A. N. Y.): "The order staying the action in the State court was a proper exercise of power, and should not be disturbed. That action was an interference with assets of the bankrupts in the custody of the bankruptcy court over which that court had previously acquired jurisdiction, and as it was brought without the leave of the court, the order staying its prosecution was properly granted."

In *re Kimball*, 3 A. B. R. 161, 97 Fed. 29 (D. C. Penn.): "Where the personal property of the bankrupt at the date of the adjudication is subject to the levy of a pending execution, the right of this court to enjoin the execution creditor, if the execution is an unlawful preference and contrary to the provisions of the Bankrupt Act, is clear."

In *re Pittelkow*, 1 A. B. R. 475, 92 Fed. 901 (D. C. Wis.): "* * * jurisdiction exists to restrain mortgagees, for a reasonable time, from commencing foreclosure proceedings, and to order sales free from incumbrances, in special instances, after due hearing, where the rights are clear."

In *re Swofford Bros. Dry Goods Co.*, 25 A. B. R. 282, 180 Fed. 549 (D. C. Mo.): "In this case the estate of the bankrupt was and is undergoing administration in this court. The visible assets were manifestly insufficient to pay more than a comparatively small dividend upon the claims allowed. A proposition was made by the petitioner Swofford to buy the remaining assets, which included claims against himself, upon the payment to the trustee of a

sum of money sufficient to enable all creditors having provable claims to receive 37½ cents of the face thereof. The court had full power to entertain such a proposition and in its discretion to accept it. This the court did, and the contract raised by that judicial determination has been in large part executed; not wholly executed, however, for the reason that further claims may still be filed and further payments by Swofford may and will become necessary. The matter is, therefore, still in process of administration by this court, and cannot be disturbed or changed without seriously impeding the enforcement of the Act and interfering with the administration of the estate. In such case there can be little doubt of the power of this court to restrain by injunction any proceeding which will have this damaging effect."

§ 1902. Restraining Sale or Distribution under Levy Made within Four Months.—Thus, the sale or distribution of property or its proceeds under levy or seizure made within four months of the bankruptcy, while still in the hands of the officer of the court making the levy or seizure, may be restrained before the adjudication, and pending the determination as to the bankruptcy of the debtor.⁷³ And, of course, also after adjudication.

So, also, a creditor may be restrained from enforcing a nullified judgment on the ground that it constitutes a cloud on the property of the bankrupt estate, and interferes with its sale by the trustee.⁷⁴

New River Coal Land Co. v. Ruffner Bros., 21 A. B. R. 474, 165 Fed. 881 (C. C. A. W. Va.): "In the act forbidding courts of the United States to stay proceedings in a State court the courts of bankruptcy are specifically excepted and the bankruptcy law of 1898 expressly confers upon these courts the power to issue injunctions to stay proceedings within this exception. * * * The prime purpose of the Bankruptcy Act is to secure an equal distribution of an insolvent's estate among the creditors, and it is not only a power conferred upon the court in a bankruptcy proceeding to take jurisdiction of the unencumbered property of a bankrupt, but also of property to which liens attach, provided the judge of the court in bankruptcy shall determine that such property should be administered by that court. It has not unfrequently been the case that the bankrupt courts have issued injunctions to stay proceedings in a State court, to foreclose mortgages, to enforce other liens, and even to forbid State officers from proceeding with executions upon judgments, where

⁷³. See ante, "Restraining Orders and Injunctions before Adjudication," § 359; In re Hornstein, 10 A. B. R. 308, 122 Fed. 266 (D. C. N. Y.); In re Goldberg, 9 A. B. R. 156, 117 Fed. 692 (D. C. N. Y.); In re Breslauer, 10 A. B. R. 33, 121 Fed. 910 (D. C. N. Y.). See ante, "Custodians and Court Officers in Possession under Nullified Legal Liens, Not Adverse Claimants," § 1827. *Bear v. Chase*, 3 A. B. R. 746, 99 Fed. 920 (C. C. A. S. C.); In re Kimball, 3 A. B. R. 161, 97 Fed. 29 (D. C. Penn.); In re Kenney, 2 A. B. R. 494, 95 Fed. 427 (D. C. N. Y., affirmed in 3 A. B. R. 353 and 5 A. B. R. 355, and reaffirmed sub nom. *Clarke v. Larremore*, 9 A. B. R. 476, 188 U. S. 486); In re Lesser Bros., 5 A. B. R.

320 (C. C. A. N. Y., reversed, on other grounds, sub nom. *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165); *Blake v. Francis-Valentine Co.*, 1 A. B. R. 372 (D. C. Calif.): This case, however, is not to be approved to its full extent. In re Northrop, 1 A. B. R. 427 (Ref. N. Y.); In re Globe Cycle, 2 A. B. R. 447 (Ref. N. Y.); In re Chas. D. Adams, 1 A. B. R. 94 (Ref. N. Y.); In re Booth, 2 A. B. R. 770, 96 Fed. 943 (D. C. Ga.); instance, In re Oxley & White, 25 A. B. R. 656, 182 Fed. 1019 (D. C. Wash.). In re Federal Biscuit Co., 29 A. B. R. 393, 203 Fed. 37 (C. C. A. N. Y.).

⁷⁴ In re Peterson, 29 A. B. R. 26, 200 Fed. 739 (C. C. A. Ill.).

in the opinion of the judge of the bankruptcy court, it was to the interest of the general estate to do so."

§ 1903. But No Injunction Where Levy Not Made within Four Months.—But there will be no injunction granted where the lien of the levy was acquired before the four months preceding the filing of the bankruptcy petition, for such levies are not invalid.⁷⁵

§ 1904. And Injunction May Be Refused on Ground of Comity.—And a restraining order to enjoin a sale under an execution levied within the four months preceding the bankruptcy may be refused on the ground of comity, until application first be made to the court from which the levy was made.⁷⁶

§ 1904½. And Where State Officers to Be Restrained, Court Cautious.—And where it is sought to restrain a State officer, the court will proceed with great caution, and hearing will not be had on mere affidavits.⁷⁷

§ 1905. Adverse Claimants Restrained until Appropriate Action Can Be Taken.—Restraining orders may be issued by the bankruptcy courts upon adverse claimants, preserving the status quo until proper proceedings or applications can be instituted in the appropriate tribunals, although the bankruptcy courts might not have jurisdiction themselves to entertain such proceedings.⁷⁸

^{75.} In re Snell, 11 A. B. R. 35, 125 Fed. 154 (D. C. Calif.); In re Mercedes Import Co., 21 A. B. R. 590, 166 Fed. 427 (C. C. A. N. Y.).

But compare cases where a distinction has been made between execution sales and judicial sales and where sheriffs have been restrained from sale and ordered to turn over the property, although levy was made prior to the four months, the lien following the property, In re Vastbinder, 13 A. B. R. 148, 132 Fed. 718 (D. C. Penn.); In re Baughman, 15 A. B. R. 23, 138 Fed. 742 (D. C. Penn.). See ante, § 1827, note.

Compare, to same effect, analogously, Sample v. Beasley, 20 A. B. R. 164, 158 Fed. 606 (C. C. A. La.). Also compare, In re Sterlingworth Ry. Supply Co., 21 A. B. R. 341, 164 Fed. 591, 165 Fed. 267 (D. C. Pa.).

^{76.} In re Shoemaker, 7 A. B. R. 437, 112 Fed. 648 (D. C. Va.). Compare, ante, §§ 362, 1637, 1860 and post, § 2699.

^{77.} In re Bailey, 19 A. B. R. 470, 156 Fed. 691 (D. C. N. Y.); obiter, In re Dana, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.).

^{78.} In re Smith, 8 A. B. R. 55, 113 Fed. 993 (D. C. Ga.): Removing of fixtures restrained; In re Currier, 5

A. B. R. 639 (Ref. N. Y.); Bindseil v. Smith, 5 A. B. R. 40 (Court of Errors N. J.): Alleged preferential transfer of note; preferred creditor enjoined. In re Kerski, 2 A. B. R. 79 (Ref. Wis.).

In re Miller, 9 A. B. R. 274, 118 Fed. 360 (D. C. Ga.), where a mortgagee, under deed absolute in form, was restrained from selling until question of usury was settled.

In re Jackson, 2 A. B. R. 501, 94 Fed. 797 (D. C. Vt.): Restraining endorsement of note.

In re Jersey Island Packing Co., 14 A. B. R. 689, 138 Fed. 625 (C. C. A. Calif.): Selling out of corporate assets under trust deed restrained.

Contra, In re Ward, 5 A. B. R. 215 (D. C. Mass.): "To take property out of one's possession and to restrain him from dealing with it as owner are but different acts of the exercise of the same jurisdiction."

In re Berkowitz, 22 A. B. R. 233, 173 Fed. 1012 (D. C. N. J.): Restraining a corporation from selling out, where corporation simply a fiction to enable bankrupt to defraud creditors.

Instance, In re Clifford D. Mills, 25 A. B. R. 278, 179 Fed. 409 (D. C. N. Y.); also, where the bankruptcy court might have jurisdiction to en-

§ 1906. **Adverse Claimants Restrained from Interfering with Assets in Custody of Bankruptcy Court.**—Of course, adverse claimants may be restrained from interfering with assets in the custody of the bankruptcy court.⁷⁹

§ 1907. **Court Proceedings Restrained until Trustee Elected and Appropriate Action Taken.**—Court proceedings may be restrained until a trustee can be elected and appropriate action be taken by him by way of intervening in the state court or otherwise;⁸⁰ thus, as to the foreclosure of mechanics' liens, mortgages, pledges, etc.;⁸¹ thus, as to an equity suit by a judgment creditor to subject the bankrupt's interest in a spendthrift trust.⁸²

§ 1908. **Court Proceedings Enjoined Where Property in Custody of Bankruptcy Court Sought to Be Seized or Levied on.**—Court proceedings whereby it is attempted to levy upon or seize property in the custody of the bankruptcy court may, of course, be enjoined; thus, as to attempts to replevin from the custody of the bankruptcy court or to levy execution on property in its custody, or otherwise interfere with it by court proceedings;⁸³ and this is so even where the property is exempt.⁸⁴

In *re* Bluestone Bros., 23 A. B. R. 264, 174 Fed. 53 (D. C. W. Va.): "It is no longer an open question in this circuit that the jurisdiction of the Federal courts in bankruptcy is essentially exclusive, and that a District Court, as a court of bankruptcy, has power to stay proceedings of a State

certain the plenary action contemplated, In *re* Norris, 24 A. B. R. 444, 177 Fed. 598 (D. C. N. Y.), alleged fraudulent bill of sale to wife; *Pyle v. Texas, etc., Co.*, 25 A. B. R. 829, 185 Fed. 309 (D. C. La.).

Restraining a litigant in the state court from proceeding further therein is to be distinguished from restraining a court or its officers. In *re* Roger Brown & Co., 28 A. B. R. 336, 180 Fed. 758 (C. C. A. Iowa).

In *re* Blake, 22 A. B. R. 612, 171 Fed. 298 (D. C. N. Y.): Restraining order on a mortgagee in possession refused, but security required from him as to disposal of rents until appropriate action could be taken.

See similar proposition before adjudication, ante, § 365.

79. In *re* Chas. D. Adams, 1 A. B. R. 94 (Ref. N. Y.), in which case third parties, to whom the landlord had leased the premises, upon the bankruptcy of the tenant, were enjoined.

Instance (restraining landlord), In *re* Schwartzman, 21 A. B. R. 885, 167 Fed. 399 (D. C. S. C.); instance (restraining bankrupt's wife from replevin suit against trustee), *Berman v. Smith*, 22 A. B. R. 662, 171 Fed. 735 (D. C. Ga.).

80. In *re* Klein, 3 A. B. R. 174, 97

Fed. 31 (D. C. Ills.). *Obiter*, *Carling v. Seymour Lumber Co.*, 8 A. B. R. 41, 113 Fed. 483 (C. C. A. Ga.).

81. In *re* Emslie, 4 A. B. R. 126, 102 Fed. 292 (C. C. A. N. Y.); In *re* Pitelkrow, 1 A. B. R. 475, 92 Fed. 901 (D. C. Wis.); In *re* Ball, 9 A. B. R. 276, 118 Fed. 672 (D. C. Vt.); In *re* Donnelly, 26 A. B. R. 304, 188 Fed. 1001 (D. C. Ohio).

82. In *re* Tiffany, 13 A. B. R. 310, 133 Fed. 799 (D. C. N. Y.). Compare, In *re* Roger Brown & Co., 28 A. B. R. 336, 196 Fed. 758 (C. C. A. Iowa).

83. *White v. Schloerb*, 4 A. B. R. 178, 178 U. S. 542; In *re* Russell & Birkett, 5 A. B. R. 608 (Ref. N. Y.); In *re* Lemmon & Gale Co., 7 A. B. R. 291, 112 Fed. 296 (C. C. A. Tenn.); In *re* Whitener, 5 A. B. R. 198, 105 Fed. 180 (C. C. A. N. Y.); *Berman v. Smith*, 22 A. B. R. 662, 171 Fed. 735 (D. C. Ga.); Instance, In *re* Kimmel, 25 A. B. R. 595, 183 Fed. 665 (D. C. Pa.); In *re* Roger Brown & Co., 28 A. B. R. 336, 196 Fed. 758 (C. C. A. Iowa); Instance, In *re* Arden, 26 A. B. R. 684, 188 Fed. 475 (D. C. N. Y.).

84. In *re* Huddleston, 1 A. B. R. 572 (Ref. Ala.); In *re* Swofford Bros. Dry Goods Co., 25 A. B. R. 282, 180 Fed. 549 (D. C. Mo.), quoted at § 1901.

court, seeking to take away from its trustee either the property itself or to impose a lien upon it."

§ 1909. Injunction Refused Where Legal Proceedings Not Nullified by Bankruptcy, and State Court Prior in Custody.—Injunction will be refused, where it is not asked for merely to give time for a trustee to be elected and to intervene to protect creditors' rights, but is asked on the ground of paramount jurisdiction of the bankruptcy court, where the state court has prior custody of the res and the legal proceedings themselves are not void.⁸⁵

Thus foreclosure suits instituted within the four months period will not be restrained; nor, a fortiori, those instituted before the four months period.⁸⁶

And this has been held even as to legal proceedings instituted after bankruptcy adjudication, where actual possession has not been taken by a bankruptcy officer.⁸⁷

§ 1909½. Foreclosure Enjoined Where Actual Possession Afterwards Acquired by Bankruptcy Court.—However, if actual possession of the property has not been taken in the foreclosure proceedings or if actual possession has been surrendered by the state court to the bankruptcy court, then the bankruptcy court acquires complete jurisdiction and may enjoin the further prosecution of the foreclosure suit, and itself determine the right of lienholders and other parties, and sell free of liens.⁸⁸

§ 1910. Whether May Restrain Levy on Exempt Property for Other Purposes than to Interpose Discharge.—Also it has been held, but on doubtful reasoning, that injunction will be granted where the property involved is exempt and the restraining order is for the benefit of the bankrupt, but is not for the purpose of securing and interposing discharge.⁸⁹

⁸⁵. See chapter XXXII, "Jurisdiction of Bankruptcy Court Where Another Court Already Has Custody," ante, § 1586, et seq. In re Shinn, 25 A. B. R. 833, 185 Fed. 990 (D. C. N. J.); In re United Wireless Tel. Co., 27 A. B. R. 1, 192 Fed. 238 (D. C. N. J.).

⁸⁶. *Sample v. Beasley*, 20 A. B. R. 164, 158 Fed. 606 (C. C. A. La.); In re Pennell, 18 A. B. R. 909, 159 Fed. 500 (D. C. N. J.); for facts, see *Kneeland v. Pennell*, 18 A. B. R. 538, 54 Misc. 43, 104 N. Y. Supp. 498, but compare, *New River Coal Land Co. v. Ruffner Bros.*, 21 A. B. R. 474, 165 Fed. 881 (C. C. A. W. Va.); and compare, also, apparently contra, In re Dana, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.).

⁸⁷. See cases cited under § 1582, ante.

Also, injunction will be granted against the prosecution of a suit where the effect of obtaining judgment

therein against the bankrupt would be to cause a surety on the bankrupt's bond in the suit to appropriate certain property of the bankrupt held by the surety as indemnity, In re Eastern Commission and Importing Co., 12 A. B. R. 305, 129 Fed. 847 (D. C. Mass.).

And injunction has been refused where it has been sought to restrain a suit in equity to wind up a corporation's affairs and to reorganize it. In re Ellsworth, 23 A. B. R. 284, 173 Fed. 699 (D. C. N. Y.), quoted at §§ 153, 158, 159, 305.

⁸⁹. In re Dana, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.), quoted at § 1796.

⁹⁰. In re Tune, 8 A. B. R. 285, 115 Fed. 906 (D. C. Ala.); In re Huddleston, 1 A. B. R. 572 (Ref. Ala.). Contra, impliedly, *White v. Thompson*, 9 A. B. R. 653, 119 Fed. 868 (C. C. A. Ala.). Contra, impliedly, *First Nat. Bank of Sayre v. Bartlett*, 21 A. B. R. 88, 35 Pa. Super. Ct. 593.

§ 1910 $\frac{1}{2}$. **Attempts to Control Trustee's Administration by Proceedings in Other Courts.**—The trustee's administration of the estate and the exercise of his discretion are not to be interfered with by proceedings brought in other courts.⁹¹

Thus, the bankrupt will not be permitted to maintain an injunction suit in the state court to prevent the trustee from carrying out a compromise of a controversy with the bankrupt's wife.⁹²

Thus, also, the plaintiff in a suit for infringement of a patent may not have injunction against the receiver or trustee in bankruptcy of the defendant (who has been adjudged bankrupt in the meantime) to prevent the paying out of the funds in the course of the administration of the bankrupt's assets, such application being properly addressed, rather, to the bankruptcy court in charge of the administration.⁹³

American Graphophone Co. v. Leeds & Catlin Co., 23 A. B. R. 337, 174 Fed. 158 (C. C. N. Y.): "It is not for this court to say what moneys the receiver shall or shall not pay out. All questions as to priority of claims and as to payment of moneys in the custody of the District Court should be submitted to that court for determination. If the claim be one not provable in bankruptcy, presumably that court will make no provision for its payment. If it be a provable claim, it is equally presumable that whatever funds there may be in the hands of receiver, over and above the expenses of administering the estate, will be retained, until all provable claims are liquidated and all questions of priority (if any arise) are determined. The whole matter is exclusively in the jurisdiction of the bankruptcy court."

In such event the bankruptcy court will direct the bankruptcy receiver or trustee not to pay out any dividends without notice to the defendant in the pending patent case.⁹⁴

§ 1911. **Suits in Personam against Receiver, Trustee or Marshal for Wrongful Seizure Not Restrained.**—But a suit in personam in a state court individually against a receiver, trustee or marshal in bankruptcy for trespass for wrongful seizure of third parties' goods will not be restrained, as a rule, where such suit does not attempt to sequester property.⁹⁵

In one case the lower court restrained a landlord from prosecuting an independent suit in personam for trespass, claiming that he was endeavoring in this indirect way to recover rent for use and occupation, having delayed

91. *In re Kranich*, 23 A. B. R. 550, 174 Fed. 908 (D. C. Pa.). Also, see ante, § 1788 $\frac{1}{2}$.

92. *In re Kranich*, 23 A. B. R. 550, 174 Fed. 908 (D. C. Pa.). Also, see ante, § 1788 $\frac{1}{2}$.

93. *In re Leeds & Catlin Co.*, 23 A. B. R. 679, 175 Fed. 309 (D. C. N. Y.).

94. *In re Leeds & Catlin Co.*, 23 A. B. R. 679, 175 Fed. 309 (D. C. N. Y.).

95. *Berman v. Smith*, 22 A. B. R. 662, 171 Fed. 735 (D. C. Ga.); *In re Em-*

pire Construction Co., 166 Fed. 1019 (C. C. A. N. Y., reversing S. C., 19 A. B. R. 704, 157 Fed. 495); *McLean v. Mayo*, 7 A. B. R. 115, 113 Fed. 106 (D. C. N. Car.); *In re Kanter & Cohen*, 9 A. B. R. 372, 121 Fed. 984 (C. C. A. N. Y.). Contra, *In re Mertens*, 12 A. B. R. 698, 131 Fed. 507 (D. C. N. Y.). See "Plenary Actions in Personam against Trustees and Receivers," ante, § 1781.

any presentation of a bill therefor as part of the expenses of administration until almost all the funds of the estate had been distributed,⁹⁶ but the reviewing court reversed the ruling on the ground that the action sounded in tort and that it was a question for the state court to determine whether it was not so in fact.

However, in any event it would seem to have been in that case equal laches on the trustee's part, not to have taken care of his expenses.

Such suits will be enjoined where the plaintiff has, by tacit consent and affirmative action, induced the officer to join issue with him in the bankruptcy court; in such cases the plaintiff will not be permitted to remove the controversy to another tribunal by bringing a suit therein against the officer.⁹⁷

§ 1911½. Staying Trustee's Administration of Estate.—No stay of the administration of the estate will be granted against the trustee at the suit of an unsuccessful litigant who has failed to give bond for appeal in the state court.⁹⁸

§ 1912. Ancillary Injunction in Aid of Bankruptcy Proceedings in Another District.—Ancillary injunction can be obtained in one district in aid of bankruptcy proceedings in another district,⁹⁹ unless a separate action be brought there in which the injunction would be proper.¹

§ 1913. No Enjoining of Pledgee's Sale, unless Fraud or Oppression Exist.—Pledgees and other lienholders in possession of securities upon property of the bankrupt estate will not be enjoined from selling their securities in accordance with contract, unless there be fraud or oppression.²

In re Brown, 5 A. B. R. 220, 104 Fed. 762 (D. C. Pa., distinguished in In re Jersey Island Packing Co., 14 A. B. R. 693, 138 Fed. 625): "A temporary re-

96. In re Empire Cons. Co., 19 A. B. R. 704, 157 Fed. 495 (D. C. N. Y.), reversed in 166 Fed. 1019, memo. decision.

97. In re Trayna & Cohn, 27 A. B. R. 594, 195 Fed. 486 (C. C. A. N. Y.).

98. In re Nat'l Lock & Metal Co., 19 A. B. R. 106, 155 Fed. 690 (D. C. N. Y.).

99. Acme Harvester Co. v. Beekman Co., 27 A. B. R. 262, 222 U. S. 300.

1. Bankruptcy Act, as amended 1910, § 2: "That the courts of bankruptcy, as hereinbefore defined, * * * are hereby invested * * * with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in bankruptcy proceedings * * * to (20) exercise ancillary jurisdiction over persons or property than their respective territorial limits in aid of a receiver or trustee appointed in any bankruptcy proceedings pending in any other

court of bankruptcy." Babbitt, Trustee, v. Dutcher, 23 A. B. R. 519, 216 U. S. 102, quoted at § 1705; inferentially, In re Peiser, 7 A. B. R. 690, 115 Fed. 199 (D. C. Pa.). Compare, Horskin v. Sanderson, 13 A. B. R. 101, 132 Fed. 415 (D. C. Vt.). Contra, In re Williams, 9 A. B. R. 741, 120 Fed. 38 (D. C. Ark.). Also, compare, § 1705.

2. See ante, § 760, et seq. Contra, inferentially, In re Cobb, 3 A. B. R. 129, 96 Fed. 821 (D. C. N. Car.), wherein the court seems to consider that pledgees in possession at the time of bankruptcy must nevertheless submit their securities to the bankruptcy court. This case was decided, it must be remembered, before the decision of the U. S. Supreme Court in *Bardes v. Bank*, 4 A. B. R. 163, 178 U. S. 524. In re Mayer, Leslie & Baylis, 19 A. B. R. 356, 157 Fed. 836 (C. C. A. N. Y.). Compare, In re Searles, 29 A. B. R. 635, 200 Fed. 893 (D. C. N. Y.).

straining order was issued, forbidding a sale under any circumstances, and it is now to be determined whether the court has the power to make the order prayed for, or any other order interfering with the creditors' right to sell.

"I do not pass upon the question, whether the court may interfere to prevent a fraudulent or oppressive exercise of such a right. No such exercise is threatened in the present case. It is agreed that the creditors intend to deal fairly with the property pledged."

Inferentially, *In re Mertens*, 15 A. B. R. 362, 142 Fed. 445 (C. C. A. N. Y., reversing 14 A. B. R. 226, and itself affirmed sub nom. *Hiscock v. Varick Bk.*, 18 A. B. R. 6, 206 U. S. 28): "The present Act provides that the value of his security may be determined, among other methods, by converting it into money, pursuant to his contract rights, and thus if he has enforced it as the contract with the debtor allowed, he is permitted to prove the unsatisfied balance of his claim. Section 57, subdivision h, prescribes several modes of valuation, and the one referred to is exclusive of the others and is superfluous and useless unless it is intended to authorize the creditor without interference by the trustee or the court to value his own security, provided he turns it into money, 'according to the terms of the agreement pursuant to which' it was delivered to him."

And where the possession of the pledgee or other lienholder is not exclusive of the bankrupt, the bankruptcy court may enjoin.³

In re Jersey Island Packing Co., 14 A. B. R. 689, 142 Fed. 445 (C. C. A. Calif.), wherein the court held, that under § 2, a court of bankruptcy has jurisdiction to restrain a sale, where all the property of an alleged bankrupt corporation is about to be sold, at the instance of its treasurer, to obtain satisfaction of debts owing to him and his wife, secured by trust deeds covering all the property; and a restraining order should be granted where such sale would extinguish the bankrupt's equity of redemption, since by selling the property under the direction of the bankruptcy court the interests of all parties would be protected. The court in this case held that the rules protecting liens do not extend to a protection of the contract remedies for enforcing such liens; and said:

"It is true that the Bankruptcy Act provides that liens such * * * shall not be affected by bankruptcy but that is far from saying that such lienholders may, after the commencement of proceedings in bankruptcy against the debtor, proceed to enforce their liens or contracts in the manner prescribed in the instruments which create them; and this is true whether such lien is an ordinary mortgage, or a deed of trust with provision for a strict foreclosure by a notice and sale. The provision of the Bankruptcy Act that such a lien shall not be affected by the bankruptcy proceedings has reference only to the validity of the lienholder's contract. It does not have reference to his remedy to enforce his

3. *In re Miller*, 9 A. B. R. 274, 118 Fed. 360 (D. C. Ga.), where the grantee of a deed absolute on its face but held as security was enjoined from sale. But compare, *In re Mertens*, 12 A. B. R. 698, 131 Fed. 507 (D. C. N. Y.).

But adverse claimants may not be enjoined from prosecuting to judgment in the state court suits against sureties holding funds of the bankrupt as indemnity, *Jacquith v. Rowley*, 9 A. B. R. 525, 188 U. S. 620 (affirming *In re Franklin*, 6 A. B. R. 285, 106

Fed. 666), although adverse claimants may be enjoined from prosecuting to judgment in the state court suits against the bankrupt himself where the bankrupt has given such indemnity to his surety and where the effect of a judgment against the bankrupt would be to cause the appropriation of the indemnity by the surety to meet the obligation of the surety to the creditor. *In re Eastern Commission and Importing Co.*, 12 A. B. R. 305, 129 Fed. 847 (D. C. Mass.).

right. The remedy may be altered without impairing the obligation of his contract, so long as an equally efficient and adequate remedy is substituted. Every one who takes a mortgage, or deed of trust intended as a mortgage, takes it subject to the contingency that proceedings in bankruptcy against his mortgagor may deprive him of the specific remedy which is provided for in his contract."

§ 1914. Injunction Where Legal Action Requisite to Fix Liability of Sureties.—Injunction may be refused to restrain third parties from taking legal action requisite to fix the liability of persons secondarily liable for the bankrupt.⁴

Thus it has been refused to the trustee where judgment is necessary to fix the liability of a surety on an attachment bond.⁵

In *re Mercedes Import Co.*, 21 A. B. R. 590, 166 Fed. 427 (C. C. A. N. Y.), reversing S. C., 20 A. B. R. 648, 166 Fed. 427): "The district judge was not obliged to grant the stay under § 11 of the Bankruptcy Act, but did so because he thought that the creditor had no better equity against the surety than he had against the bankrupt. As the trustee in bankruptcy has no interest whatever in the claim against the surety, we think the creditor's rights and equities are questions to be disposed of by the State court. * * * We think the court in which the action is pending should be left free to take whatever steps it thinks equitable in the premises in accordance with its own practice, and the order granting the stay is therefore reversed."

Thus, it has been refused where judgment and return of execution unsatisfied against a corporation was necessary to fix the secondary liability of the stockholders.

In *re Remington Auto. & Motor Co.*, 9 A. B. R. 533, 119 Fed. 441 (D. C. N. Y.): "Some of the creditors of this alleged bankrupt corporation are now seeking to put their respective claims in judgment, issue execution, and thus place themselves in a position to bring an action in equity of the nature and for the purpose mentioned. If this preliminary action be necessary when bankruptcy has intervened, the injunction should not be made permanent or continued, for if such a liability exists, and it can be enforced only by a creditor with judgment and execution returned unsatisfied, or by the trustee, when appointed, after a creditor or creditors have put themselves in this position, then to grant or make permanent this injunction will be to deprive the creditors of their rights."

But it is likewise true that injunction may be granted. And proceedings subsequent to judgment may be enjoined where the suit itself has been allowed to proceed to judgment to fix the liability of sureties.

A suit will not be allowed to proceed to judgment in order to fix the liability of a surety on an attachment bond where the attachment was levied within the four months if the surety holds indemnity from the bankrupt,

4. In *re Ennis & Stoppani*, 22 A. B. R. 679, 171 Fed. 755 (D. C. N. Y.), quoted at § 1524; In *re Remington Auto. & Motor Co.*, 9 A. B. R. 533, 119 Fed. 441 (D. C. N. Y.). Compare, In *re Engle*, 5 A. B. R. 372, 374, 105 Fed. 893 (D. C. Penn.). See, also,

subjects of "Rights of Creditors against Sureties, etc.," § 1524, and "Stay of Actions against Bankrupt," § 2711 and § 2712.

5. In *re Ennis & Stoppani*, 22 A. B. R. 679, 171 Fed. 755 (D. C. N. Y.), quoted ante, § 1524.

given contemporaneously with his becoming surety, to which the surety might resort for indemnification.^{5a}

§ 1915. No Restraining Order to Prevent Proceeding with Levy on Exempt Property after Same Set Apart.—Likewise it has been held that no restraining order will be granted to prevent a creditor from proceeding with his levy on exempt property, after the property has been set apart.⁶

§ 1916. Bankruptcy Petition "Caveat to All the World" and "Attachment and Injunction."—It is said that the filing of the bankruptcy petition is a caveat to all the world and operates as an attachment and an injunction.⁷

However, the maxim quoted is not to be literally relied on as furnishing a working rule for actual practice. It is misleading to say in all instances that the mere "filing" of a petition is "in effect an attachment." Such "filing" would operate as an attachment only where the property involved is in the custody of the bankruptcy court or is brought therein either through being in the possession of the bankrupt or of a receiver or marshal of the court, but the mere "filing" certainly would not operate as an "attachment" under any doctrine, if the bankruptcy court had no such custody.⁸

In re Rathman, 25 A. B. R. 246, 183 Fed. 913 (C. C. A.): "But counsel insist here that the filing of the petition in bankruptcy 'is a caveat to all the world and in effect an attachment and injunction,' and they cite *Mueller v. Nugent*, 184 U. S. 1, 14, 7 Am. B. R. 224, and the numerous opinions of the courts that repeat this statement. But the later decisions of the Supreme Court adjudge that this statement applies only to parties who have no substantial claim of a lien upon or a title to the property of the bankrupt, and that against those who have such claims of existing liens or titles when the petition in bankruptcy is filed, that filing is neither a caveat nor an attachment, that it creates no lien and that until the bankruptcy court by some act of one of its officers takes actual possession of the property, or makes such claimants parties to the pro-

5a. In re Federal Biscuit Co., 29 A. B. R. 393, 203 Fed. 37 (C. C. A. N. Y.).

6. In re Jackson, 8 A. B. R. 596, 116 Fed. 46 (D. C. Pa.). Compare, ante, "Exemptions," § 1032.

7. *Mueller v. Nugent*, 7 A. B. R. 224, 184 U. S. 1; *Whitney v. Wenman*, 14 A. B. R. 51, 198 U. S. 539; In re Gutman & Wenk, 8 A. B. R. 252 (D. C. N. Y.); In re Mertens, 12 A. B. R. 698, 131 Fed. 507 (D. C. N. Y.); In re Reynolds, 11 A. B. R. 758, 127 Fed. 760 (D. C. Mont.); In re Reynolds, 13 A. B. R. 250, 133 Fed. 584 (D. C. Mont.); In re Breslauer, 10 A. B. R. 33, 121 Fed. 910 (D. C. N. Y.); In re Briskman, 13 A. B. R. 57, 132 Fed. 201 (D. C. N. Y.); In re Jersey Island Packing Co., 14 A. B. R. 691, 138 Fed. 135 (C. C. A. Calif.); In re Weinger, Bergman & Co., 11 A. B. R. 424, 126

Fed. 875 (D. C. N. Y.). In effect, In re Abrahamson v. Bretstein, 1 A. B. R. 44 (Ref. N. Y.). See ante, § 1215. *Acme Harvester Co. v. Beekman*, 222 U. S. 300, 27 A. B. R. 262, quoted at § 1270 9/10; obiter, In re Zotti, 26 A. B. R. 234, 186 Fed. 84 (C. C. A. N. Y.), affirming S. C., 23 A. B. R. 304.

See discussion ante, § 1270 9/10, "Maxim That Filing of Petition a Caveat, Attachment and Injunction."

8. Compare, ante, § 1270 9/10; also see *Fidelity Trust Co. v. Gaskell*, 28 A. B. R. 4, 95 Fed. 864 (C. C. A. Mo.), quoted at § 1270 9/10; compare, In re Mullen, 21 A. B. R. 229, 101 Fed. 413 (D. C. Mass.); compare, In re Mertens, 15 A. B. R. 369, 144 Fed. 818 (C. C. A. N. Y.); In re Rathman, 25 A. B. R. 246, 183 Fed. 913 (C. C. A.).

ceeding by some order or process, or notice of the proceeding comes to them, their liens, titles and remedies are unaffected thereby and they are strangers to the proceedings.

"These propositions, the authorities above, and many others cited by counsel for the trustee and examined, fail to convince that the filing of the petition in bankruptcy and the adjudication, without any acquisition or demand of possession of the property by any officer of the bankruptcy court, or any notice of the proceeding therein to the mortgagee, the State court, its receiver, or the purchaser at its foreclosure sale, conferred upon it jurisdiction to determine by a summary proceeding the merits of Booth's adverse claim to the mortgage liens upon the property at the time the petition in bankruptcy was filed, or his adverse claim at the time the petition for the order to show cause was filed to the moneys which the trustee thereby seeks to recover from him for the conversion of the personal property, and to the real estate subject to the possible right of the trustee to redeem from the foreclosure sale thereof by paying the amount Booth paid therefor at that sale.

"If the commencement of bankruptcy proceedings without more, without any act of the bankruptcy court, or any of its officers, to give notice to adverse claimants, or to reduce the property claimed to belong to the bankrupt to the possession of the officers of that court as his property gives it constructive possession, and hence a legal custody that enables it to determine by summary proceedings the merits of adverse claims to liens and titles to such property in the actual possession of others, then no case could ever arise in which any other court could have jurisdiction by plenary suit to determine the merits of such claims, for in every case a bankruptcy proceeding is commenced and the only ground on which the jurisdiction to determine summarily the merits of such claims is sustained, is that the bankruptcy court's legal custody of the property excludes the jurisdiction of every other court and gives it the power to determine summarily all claims to liens upon, or interests in, the property in such custody. But this theory flies in the face of the settled rule repeatedly announced by the Supreme Court that the actual possession by the bankruptcy court is the indispensable condition of its exclusive and of its summary jurisdiction here."

§ 1917. No Injunction before Filing of Bankruptcy Petition to Preserve Status Quo.—But restraining orders will not be issued before the filing of a bankruptcy petition, either in the state or the bankruptcy courts, expressly to preserve the status quo until a bankruptcy petition can be filed: such ground is not in itself ground for a restraining order, although a restraining order may be granted in a creditor's suit brought before the filing of any bankruptcy petition which may have that effect as an incident.⁹

Clothing Co. v. Hazle, 6 A. B. R. 265, — Mich. —: "It is apparent that the object of this bill was merely to preserve an estate until a time should come when it could be administered under the new law, which at the time the bill was filed did not authorize the Federal Courts to interfere. It is claimed that, as these courts were powerless to protect creditors under the Bankruptcy Act, the State courts must have the power. This does not impress us as being a

9. *Ellis v. Hays Saddlery & Leather Co.*, 8 A. B. R. 109 (Kans. Sup. Ct.); *Victor v. Lewis*, 1 A. B. R. 667, 53 N.

Y. Supp. 944. Contra, *In re Valentine*, 1 A. B. R. 372 (D. C. Calif.).

sound theory. The rights and remedies in such cases under the State law were settled. They existed and were open at this time. But counsel say that they might be superseded or supplemented for the four months following July 1st by another remedy, so that they might, if they chose, avail themselves of a prospective remedy afforded by the Bankruptcy Act. We see no better reason why this should be than that an injunction should heretofore have been issued, in any case of fraud and danger, to impound the estate until creditors' claims should mature, judgment be obtained, execution issued and returned, to the end that a creditors' bill might be effectively filed. The exigency is as great in such a case as this, yet no one has heard of such a proceeding being permitted."

§ 1917½. Injunction after Sale by Trustee.—It has not been authoritatively decided whether injunction may issue after a trustee's or receiver's sale, to protect the purchaser in his rights.¹⁰

§ 1918. Referee Has Jurisdiction to Issue Restraining Order, Except upon Courts or Court Officers.—The referee has jurisdiction in general to issue the restraining order.¹¹

Obiter, In re Rochford, 10 A. B. R. 615, 124 Fed. 182 (C. C. A. S. Dak.): "That portion of that order which enjoined the petitioners from threatening the purchases at the sale with their adverse claims to the property may have overstepped and probably did pass beyond the limits of the authority of the referee."

But the referee has no jurisdiction to enjoin the proceedings of a court, or of an officer thereof.¹²

Restraining a litigant in the state court from proceeding further therein, however, is to be distinguished from restraining the court or its officers.¹³

§ 1919. Petition Requisite and to Be Filed in Bankruptcy Proceedings Themselves.—The injunction is only to be granted upon proper petition.¹⁴ The petition is to be filed in the bankruptcy proceedings themselves. Thus, after adjudication it is usually to be filed before the referee, except in cases where a court or court officer is to be restrained. Before ad-

¹⁰ Query, In re Bluestone Bros., 23 A. B. R. 264, 174 Fed. 53 (D. C. W. Va.).

¹¹ In re Adams, 14 A. B. R. 23, 134 Fed. 142 (D. C. Conn.); In re Booth, 2 A. B. R. 770, 96 Fed. 943 (D. C. Ga.); inferentially, In re Huddleston, 1 A. B. R. 572 (Ref. Ala.); inferentially, In re Kerski, 2 A. B. R. 79 (Ref. Wis.), which case, however, states the power too broadly. In re Steuer, 5 A. B. R. 209, 104 Fed. 976, 980 (D. C. Mass.); In re Martin, 5 A. B. R. 423, 105 Fed. 753 (D. C. N. Y.); impliedly, In re Wilkes, 7 A. B. R. 574, 112 Fed. 975 (D. C. Ark.); In re Moody, 12 A. B. R. 718, 131 Fed. 525 (D. C. Iowa); In re Currier, 5 A. B. R. 639 (Ref. N. Y.); inferentially, In

re Rochford, 10 A. B. R. 610, 124 Fed. 182 (C. C. A. S. Dak.).

It is doubtful, however, whether an adverse claimant should be restrained from proclaiming his adverse claim to prospective purchasers, at any rate by the referee.

See, also, *supra*, § 527.

¹² Gen. Order No. XII. In re Seibert, 13 A. B. R. 348 (D. C. N. J.); In re Steuer, 5 A. B. R. 209, 104 Fed. 980 (D. C. Mass.). Inferentially, contra, In re Huddleston, 1 A. B. R. 572 (Ref. Ala.). See ante, § 528.

¹³ In re Roger Brown & Co., 28 A. B. R. 336, 196 Fed. 758 (C. C. A. Iowa).

¹⁴ See instances under the various headings of this division.

judication the petition is to be filed with the district clerk and may only be heard by the judge unless, of course, he be absent or otherwise unable to hear it, in which event the referee is vested with authority to hear it. The petition should be entitled in the bankruptcy case itself. But it is a separate proceedings within the bankruptcy proceedings, and should not form part of the bankruptcy petition itself, for fear of multifariousness.¹⁵

The entitling of the petition itself, without allegations in the body, sufficiently shows the pendency of the proceedings in bankruptcy within the district.¹⁶

§ 1920. Petition to Be Verified.—The petition for the injunction should be verified; but it may be verified by an attorney, where the moving papers show the moving creditors live at a distance, and state the reason for the attorney's verifying.¹⁷

§ 1921. Notice to Be Given, unless for Good Cause Dispensed with.—Notice must be given of the filing of the petition for the injunction,¹⁸ unless, for good cause shown, the injunction is granted without notice, under the usual rules of practice.¹⁹

But verbal notice of an order of injunction already granted is sufficient to subject the parties enjoined to punishment for contempt for its disobedience.²⁰

DIVISION 8.

CONTEMPTS FOR INTERFERENCE WITH CUSTODY OF BANKRUPTCY COURT.

§ 1922. Jurisdiction to Punish for Contempts for Interference with Custody.—The bankrupt or a third person interfering with property in the custody of the bankruptcy court after the filing of the bankruptcy petition, may be punished for contempt.²¹

In re Arnett, 7 A. B. R. 522, 112 Fed. 776 (D. C. Tenn.): "But there remains the necessity of vindicating the authority of the law and practice of the court in the matter of the contempt of the bankrupt and the mortgage trustee of Godfrey Frank & Co. in surrendering the property held by the bankrupt to the mortgage trustee after the petition in bankruptcy had been filed. The bankrupt should either have kept the property for the bankruptcy trustee or surrendered it under the rules to the referee as caretaker."

15. See ante, § 361.

16. In re Goldberg, 9 A. B. R. 156, 117 Fed. 692 (D. C. N. Y.).

17. In re Goldberg, 9 A. B. R. 156, 117 Fed. 692 (D. C. N. Y.).

18. Beach v. Macon Grocery Co., 8 A. B. R. 751, 116 Fed. 143 (C. C. A.); In re Steuer, 5 A. B. R. 209, 104 Fed. 976 (D. C. Mass.). Compare similar rule as to appointment of receivers, ante, § 383. See also, § 363.

19. Compare, In re Barrett, 12 A. B.

R. 626, 132 Fed. 362 (D. C. Tenn.); In re Steuer, 5 A. B. R. 209, 104 Fed. 976 (D. C. Mass.). See also, § 363.

20. In re Krinsky Bros., 7 A. B. R. 535, 112 Fed. 972 (D. C. N. Y.). Compare, to same effect, in plenary suits by trustees, Blake v. Nesbet, 16 A. B. R. 269 (D. C. Mo.).

21. Obiter, Carter v. Hobbs, 1 A. B. R. 215, 92 Fed. 594 (D. C. Ind.). See post, § 2331½.

§ 1923. Restraining Order Not Prerequisite.—Contempt proceedings will lie for interference with assets already in the control of the bankruptcy court, without the issuance of a restraining order.²²

Clay v. Waters, 24 A. B. R. 293, 178 Fed. 385 (C. C. A. Mo.): "Attention is sharply challenged to the fact that there was no restraining order or specific injunction against the taking and conversion of the property of the bankrupt by this defendant. But the filing of the petition in bankruptcy and the adjudication which followed it embodied in themselves a commanding injunction of the court against the interference of the defendant with and his concealment and removal from the trustee and the court of any of the property of the bankrupt. Against the defendant and against all others who had no valid lien upon or interest in that property at the time of the adjudication, the injunction and command of the court against such interference and removal and notice thereof to all the world were embodied in the injunction and issued therewith by the settled law of the land. The decisions of the Supreme Court in *York Manufacturing Co. v. Cassell*, 15 Am. B. R. 633, 201 U. S. 344, 353, and *Hiscock v. Varick Bank of New York*, 18 Am. B. R. 1, 206 U. S. 28, 41, cited for the defendant, merely hold that this *caveat* and injunction do not deprive those who have valid titles to or liens upon the property claimed by the bankrupt at the time the petition is filed of those liens or titles. They do not in any way modify this general rule or diminish its controlling force in all cases like that in hand, wherein the intermeddler had no claim upon or interest in the bankrupt's property at the time of the adjudication. The seizure of the money of the bankrupt after the adjudication and its concealment by the defendant in his name in real estate and promissory notes and his transfer of this real and personal property to innocent third parties to withdraw it from the jurisdiction of the court below and to defeat its coming decree after he was notified by the commencement of the suit to turn it over to the trustee were repeated disobediences and resistances of the injunction and command of the court, and constituted contempts of that court well within the terms of § 725, Rev. Stat."

22. Instance, *In re Arnett*, 7 A. B. R. 522, 112 Fed. 770 (D. C. Tenn.): Bankrupt surrendering assets to creditor after filing his petition and creditor accepting same, both fined.

Instance not contempt, mere threats to interfere: *In re McBryde*, 3 A. B. R. 729, 99 Fed. 686 (D. C. N. Car.),

in which case the sheriff and deputies did not levy nor interfere with the property of the bankrupt after adjudication, but merely threatened to do so. The court held that this did not constitute contempt. See post, § 2331½.

PART VI.

CONVERTING THE ASSETS INTO MONEY.

CHAPTER XXXVII.

APPRAISAL.

Synopsis of Chapter.

- § 1924. All Property of Estate to Be Appraised.
- § 1925. Only Property of Estate Need Be Appraised.
- § 1926. Appraisers to Be Disinterested.
- § 1927. And to Be Appointed by and Report to the Court.
- § 1928. Three Appraisers.
- § 1929. To Be Sworn.
- § 1930. Methods of Arriving at Appraisal Values.
- § 1930½. Reappraisal.

§ **1924. All Property of Estate to Be Appraised.**—All property of the estate must be appraised, by three disinterested appraisers, who are appointed by and report to the court.¹

The purpose of this provision is to secure for the benefit and protection of all parties concerned a designation and estimation of the property which passes into the hands of the trustee, and for which, in the first instance, he is accountable.²

A sale made without appraisalment is not, however, a nullity; it is a mere irregularity to be corrected by review.³

Robertson v. Howard, 229 U. S. 254, 30 A. B. R. 611: "As regards the alleged lack of an appraisalment and error in the description of the property covered by the certificate, contained in the published notice, we think they must in this collateral proceeding be deemed as mere irregularities, and that the order of confirmation, made by the referee, was sufficient to validate the sale under the discretionary power given to the referee by § 70b of the Bankruptcy Act. *Thompson v. Tolmie*, 2 Pet. 157, 7 L. Ed. 381."

§ **1925. Only Property of Estate Need Be Appraised.**—All the property belonging to the estate is to be appraised. This is a requirement, however, only as to property belonging to the estate. It is not requisite that property in the custody of the court but not belonging to the estate, such as exempt property, be appraised; though frequently it is desirable to appraise exempt property, whenever the exemption right is limited by value and the articles claimed as exempt approximate the limit in value.⁵

1. Bankr. Act, § 70 (b).

2. In re Gordan Supply & Mfg. Co., 13 A. B. R. 352, 133 Fed. 798 (D. C. Pa.).

3. In re Maloney, 21 A. B. R. 502 (Sup. Ct. D. of C.); In re Monsarrat (No. 2), 25 A. B. R. 820 (D. C. Hawaii).

In re Zehner, 27 A. B. R. 536, 193 Fed. 787 (D. C. La.): "Any appraisalment of the property made in the

usual course of the bankruptcy proceedings may be disregarded in selling it and the sale approved by the court, if the price is considered adequate."

5. See ante, § 1080.

But the objection that a sale was made without appraisalment cannot be raised for the first time on review. In re Gutterson, 14 A. B. R. 495, 136 Fed. 698 (D. C. Mass.).

§ 1926. Appraisers to Be Disinterested.—The appraisers must be disinterested.⁶ Thus, prospective purchasers would be disqualified.⁷ Also personal friends of the bankrupt would be disqualified, for they might be inclined to favor a low valuation for the bankrupt's sake, so that he might be able to buy in the assets. Creditors themselves would be disqualified.

Whether employees of creditors are disqualified is a question of fact in each particular case, resting much upon the discretion of the court. Remote affiliations with creditors may be disregarded.⁸

§ 1927. And to Be Appointed by and Report to the Court.—The appraisers are to be appointed by and report to the court; and it has been held to be the better practice for the court to act upon his own unfettered judgment and not to permit creditors to nominate them;⁹ although there really would seldom be any ground for objecting to nominations by the creditors, since creditors usually are simply desirous of getting the best values out of the assets, and are likely to be in a position to select the best qualified persons from among the members of the particular trades interested in the failure.

Appraisers are not to be considered as appointees nor agents of the trustee; nor is their compensation to be figured as part of the trustee's expenses. They are independent of the trustee and act as advisers of the creditors upon the matter of values, so that creditors and the court may know when the trustee has realized a fair price for the assets in his hands.

The referee has power, after adjudication and reference, to appoint appraisers;¹⁰ but before adjudication, if appraisers are to be appointed, they must be appointed by the judge;¹¹ except that, as in other matters, in the judge's absence or disability, on certificate to that effect, the referee may make the appointment.

§ 1928. Three Appraisers.—There must be three appraisers to appraise each piece of property. This does not mean that the same three must appraise all the property, nor that each piece must be appraised by a

6. Impliedly, *In re Columbia Iron Works*, 14 A. B. R. 526, 142 Fed. 234 (D. C. Mich.).

7. Compare, conversely, setting aside of sale made to an appraiser, post, §§ 1955, 1955½.

8. *In re Columbia Iron Works*, 14 A. B. R. 526, 142 Fed. 234 (D. C. Mich.).

9. *In re Columbia Iron Works*, 14 A. B. R. 526, 142 Fed. 234 (D. C. Mich.).

10. *In re Styer*, 3 A. B. R. 424, 98 Fed. 290 (D. C. Pa.); impliedly, *In re Columbia Iron Works*, 14 A. B. R. 525, 142 Fed. 234 (D. C. Mich.).

11. *In re Styer*, 3 A. B. R. 424, 98 Fed. 290 (D. C. Pa.).

Prescribed Form of Order of Ap-

pointment.—The order appointing them is prescribed by the Supreme Court and is as follows: "It is ordered that — of —, — of —, and — of —, three disinterested persons, be, and they are hereby, appointed appraisers to appraise the real and personal property belonging to the estate of said bankrupt set out in the schedules now on file in this court, and report their appraisal to the court, said appraisal to be made as soon as may be, and the appraisers to be duly sworn." However, the appraisers are not confined to the property that is "set out in the schedules." They are to appraise all the property belonging to the estate.

different set of appraisers. Sometimes property belonging to a bankrupt estate is scattered about different states, and sometimes it consists of widely differing classes of property, such that men qualified to appraise in one branch would not be qualified in another; as, for instance, real estate, hardware, a stock of groceries, patents, boots and shoes. It would be difficult to procure three appraisers who would be able to find even one in their midst for each class of assets. In some cases different sets of appraisers may be appointed for each different locality or class of goods, but always there must be three of them passing upon each piece although all three need not necessarily be expert in each line.

§ 1929. To Be Sworn.—They are presumed to be sworn well and faithfully to appraise the property before they go out to make the appraisal; but, since an appraisal probably is not complete until signed by the appraisers, it frequently happens that the appraisers go out and view the property and make their estimates first, and are sworn afterwards, the appraisal not being complete until after they have been sworn.

§ 1930. Methods of Arriving at Appraisal Values.—It is difficult to lay down hard and fast rules as to how the appraisers shall arrive at their estimates. A few propositions, however, may be safely relied on.

Appraisers must not try to guess at what the assets will bring at bankrupt sale or forced sale; the assets may be sold for three-fourths of their valuation and if the appraisers could be permitted to fix the valuation thus, the circle would be unending, for while they would be trying to guess at what the purchasers would pay, the purchasers would be giving only three-fourths of the guess, and so on. The cupidity of bargain hunters is not the proper test.

In re Prager, 8 A. B. R. 356 (Ref. Col.): "In appraising a stock of this character, the prevailing cost to the trade should be taken as the actual value. If the stock is shopworn or otherwise damaged or unseasonable, or otherwise out of date, these facts, and perhaps others of a like nature, may be considered and due allowances made for such deterioration or depreciation in value. But the appraisers have no business to anticipate or consider the cupidity of bidders who may be looking for bargains. The object of the appraisement is to inform the court and the creditors what the actual value of the property is. They are not expected to know or to guess what the property will bring at a sale. It may be sold in bulk. In that case it would no doubt have to be sold for less than cost. It may be sold in parcels. In that case it might bring more than the cost price. How it is to be sold and for how much less than its actual value are questions to be determined by the court and the creditors, not by the appraisers."

The rules for appraisal naturally must vary with each class of property. The appraisers must take into account probable customers and the extent of their demand. The general rule for the appraisal of stocks of merchandise is that the fair market value should be taken, having in view the sea-

son, the quality, the kinds and styles, the brokenness of lots and the quantities. The rules for appraising the assets of a going concern must, in the nature of things, differ from those applicable to the valuation of its component parts; and so, frequently, it is advisable to have the appraisal returned alternatively, as a going concern and as dead assets. There is no rule against this manner of appraisal and it certainly is natural and rational, and is of much assistance to creditors and purchasers alike.

Likewise, in most cases of stocks of merchandise, the appraisal should be returned both at what the articles would bring if sold at retail and what the stock would bring if sold in bulk as an entirety. The values should be different, for by selling in bulk the expense of sale is cut down, though the gross price realized is likely to be lower.

The particularity with which an appraisement of the bankrupt's property is to be made must depend somewhat upon circumstances, but it must be general rather than special, only such particularity being given as will be sufficient to reasonably identify the property in character and quantity and give a fair idea of its value.¹²

§ 1930½. **Reappraisal.**—Reappraisal may be ordered. Although there are no special rules laid down in the bankruptcy decisions as to what circumstances will warrant reappraisal, yet, in view of the fact that the judgment of the appraisers is sought precisely in order that creditors may be informed as to what price the trustee ought to obtain for the assets, it would seem that the mere fact that the trustee reports his inability to sell at the appraised value would be, alone, insufficient to warrant a setting aside of the appraisal and an ordering of a reappraisal. Showing certainly should also be made of mistake or incorrect methods in arriving at the values, to warrant reappraisal; and the better practice, undoubtedly, is to call in the appraisers themselves. Otherwise where the trustee is indolent, or inefficient, appraisals are likely to be disregarded, and creditors to lose the benefit of the independent judgment of experienced men as to the value of the assets of the estate.

¹². In re Gordon Supply & Mfg. Co.,
13 A. B. R. 352, 133 Fed. 798 (D. C.
Pa.).

Appraisers' Fees.—See post, § 2121.

CHAPTER XXXVIII.

SALE OF ASSETS.

Synopsis of Chapter.

- § 1931. Sale to Be on Petition and Order.
- § 1932. Equity Rules Followed Where Act, Forms and Orders Silent.
- § 1933. Special Orders as to Manner of Sale.
- § 1934. As to Auctioneers Conducting Sale.
- § 1935. Whether Sale to Be for Cash.
- § 1936. Bids Both in Bulk and Parcels with Acceptance of Greater Aggregate.
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- § 1941. Who May File Petition to Sell: Trustee, Receiver, Marshal, Bankrupt.
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- § 1946. Before Adjudication Judge Alone to Order Sale, unless Unable to Act.
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- § 1949. Sale Subject to Approval and to Be for Seventy-Five per Cent.
- § 1950. Trustee's Sale, a Judicial Sale.
- § 1951. And Court Has Greater Discretion than in Other Sales.
- § 1952. "Gross Inadequacy" Sufficient to Refuse Confirmation.
- § 1953. But Mere Inadequacy, or Merely a Better Offer, Insufficient.
- § 1954. Stifling of Competition; Misconduct of Trustee or Unfairness to Bidders.
- § 1954½. Injury to Innocent Parties, Avoidance of Confusion, etc.
- § 1955. Bankrupt May Be Bidder.
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- § 1955½. Reorganization Committees, etc., as Purchasers.
- § 1955¾. Selling Rights of Action.
- § 1956. May Accept Bid of Less than Seventy-Five per Cent.
- § 1957. Inherent Power to Refuse Confirmation or to Set Aside, Even Where Not Expressly Ordered "Subject to Approval."
- § 1957½. Purchaser Entitled to Hearing.
- § 1958. Formal Approval Not Always Essential to Confirmation.
- § 1959. "Caveat Emptor."
- § 1960. Discretion in Approving or Setting Aside Sale Not to Be Revised, Except for Abuse.
- § 1961. Resale.
- § 1962. Summary Power to Compel Purchaser to Complete Sale.
- § 1962½. Plenary Action against Purchasers.

§ 1931. **Sale to Be on Petition and Order.**—No sale should be made without first filing a petition and procuring an order to sell from the

court.¹ The receiver or trustee should obtain an order of sale as a matter of protection.²

But confirmation may cure the failure to get a previous order.

In *re Harvey*, 10 A. B. R. 568, 122 Fed. 745 (D. C. Pa.): "The sale was without previous authority from the court, but it was duly confirmed, and the confirmation was equivalent to a prior order."

Various forms have been prescribed by the Supreme Court for leave to sell, and since the forms and orders virtually amount to advance interpretations of the statute itself, the inference is proper that sales are to be made only on petition.

But compare, In *re Fulton*, 18 A. B. R. 591, 153 Fed. 664 (D. C. N. Y.): " * * * But nevertheless it is apparently certain that a sale of a chattel real by a receiver without the express direction of the court conveys no title. The defect in the sale cannot be cured by a motion to confirm the sale and to quiet adverse claims to the property sold."

§ 1932. Equity Rules Followed Where Act, Forms and Orders Silent.—The procedure, where not otherwise prescribed by the Bankruptcy Act, Forms or Orders, will follow the usual procedure in equity in the United States Courts wherever the same is applicable.³

In *re Britannia Min. Co.*, 29 A. B. R. 472, 203 Fed. 451 (C. C. A. Wis.): "Undoubtedly the Act of March 3, 1893, applies not only to federal courts then in existence, but also to those subsequently created, unless something in the organic act exempts them; and governs as well any possible new forms of judicial sales under decrees as foreclosure, execution, and partition sales then known. But, in our judgment, the Act of 1893 has no application to trustees' sales of the assets of bankrupt estates * * *." Quoted further at § 1939.

But where the Bankruptcy Act itself gives the right to sell, or the method of selling, its provisions will prevail over those of the Act of Congress of 1893, 27 U. S. Stats. 751.^{3a}

In *re Edes*, 14 A. B. R. 382, 135 Fed. 595 (D. C. Me.): "Under the general rules of construction, it must be held that, if Congress had intended to

1. See ante, § 386½. Inferentially, In *re Harvey*, 10 A. B. R. 568, 122 Fed. 745 (D. C. Pa.); In *re Fulton*, 18 A. B. R. 591, 153 Fed. 664 (D. C. N. Y.), quoted at § 386½.

What petition to sell free from liens should contain. Compare, In *re Granite City B'k*, 14 A. B. R. 408, 137 Fed. 818 (C. C. A. Iowa, affirming In *re Wilka*, 12 A. B. R. 727).

Stipulation between receiver and adverse claimant as to sale of property in adverse claimant's possession. See *Ommen, Trustee, v. Talcott*, 23 A. B. R. 572, 175 Fed. 261 (D. C. N. Y.). Compare, *Ommen, Trustee, v. Talcott*, 26 A. B. R. 689, 188 Fed. 401 (C. C. A.

N. Y., reversing in part S. C., 23 A. B. R. 572, 175 Fed. 261).

Order Directing Purchaser to Pay Appraisal Values Where Offer Made by Purchaser Is Simply to Pay "Lowest Market Prices."—In *re Jungmann*, 26 A. B. R. 401, 186 Fed. 302 (C. C. A. N. Y.).

2. *Obiter*, In *re Carothers*, 27 A. B. R. 921, 193 Fed. 687 (D. C. Pa.).

3. Compare, ante, §§ 1757, 1758, 1759, 1759½. And that the equity rules can not, in general, be changed by stipulation, see *Vitzthum v. Large*, 20 A. B. R. 666, 162 Fed. 685 (D. C. Iowa), quoted at § 1759½.

3a. Quoted at § 1939 note.

limit the sales of property under the Bankrupt Law to the provisions of the Act of 1893, it would have said so in clear terms. The only limitation imposed by the bankruptcy statute is that such sales must be 'subject to the approval of the court.' * * * The Bankruptcy Law is the last expression of the legislative will upon the subject. It clearly does not intend to limit the method of sales of property by the provisions of the Act of 1893. If it did, referees and trustees would be very much limited and harassed in their disposition of property—particularly in the disposition of perishable property—and the purpose of the law would be in a large degree defeated. A new statute which affirmatively grants a larger jurisdiction or power or right is held to prevail over any prior statute by which a limited power or jurisdiction or right less ample has been granted. Sutherland on Statutory Construction, § 254, and cases cited. It must be held that the Bankrupt Law, in ordering sales, is not limited by the Act of March, 1893."

§ 1933. Special Orders as to Manner of Sale.—The bankruptcy court may make special orders with regard to the manner of conducting sales, provided, of course, they do not contravene the provisions of the Bankruptcy Act, or of the orders in bankruptcy.⁴

Thus, the court may order the trustee to solicit bids and may provide for the making and hearing of objections thereto preliminary to sale.

§ 1934. As to Auctioneers Conducting Sale.—Thus, undoubtedly, in a proper case an experienced auctioneer may be employed.⁵ And the employment of special commissioners has been approved, in one case.⁶

But the manifest spirit of economy of the Bankrupt Act discourages the employment of auctioneers and others, except when absolutely necessary. It is usually one of the business duties of the trustee, for which he is presumably elected, to conduct the sales of the bankrupt's assets.⁷

At any rate, a local rule prescribing that sales shall be made by an official auctioneer may be dispensed with by the court.⁸

§ 1935. Whether Sale to Be for Cash.—The courts have not decided whether the sale must, in all instances, be for cash.

Compare, *In re Shoe & Leather Reporter*, 12 A. B. R. 284, 129 Fed. 588 (C. C. A.): "The District Court provided that the minimum bid should be \$60,000, and that the purchaser might pay five-sixths of the purchase money in bonds secured by the mortgage referred to. The other sixth, being not less than \$10,000, it ordered to be paid in cash. The petitioners claim that the District Court had no power to order any portion of the purchase price to

⁴. *In re Chandler*, 28 A. B. R. 89, 194 Fed. 944 (C. C. A. Ill.).

⁵. See post, "Costs of Administration," § 2037. *In re National, etc., Co.*, 27 A. B. R. 92, 193 Fed. 232 (D. C. Mass.).

⁶. *Sturgis v. Corbin*, 15 A. B. R. 545, 141 Fed. 1 (C. C. A. W. Va.).

⁷. See post, "Costs of Administration," § 2037.

Employment of Brokers and Agents to Procure Purchasers.—It is also

within the discretion of the court to permit the trustee to employ a broker or other agent to procure purchasers and to pay commissions to them for their services. See post, § 2037½. But such employment is likely to lead to serious abuses. *Gold v. South Side Trust Co.*; 24 A. B. R. 578, 179 Fed. 210 (C. C. A. Pa.), quoted at § 3011½.

⁸. *In re Nevada-Utah, etc., Corp.*, 28 A. B. R. 409, 198 Fed. 497 (D. C. N. Y.).

be paid in bonds, but it is plain that they cannot be prejudiced by its order in that particular, so that we need not investigate its powers in reference thereto."⁹

It would seem there would be no objection to a sale on deferred payments, if the deferred payments are properly secured and the effect is not to unduly prolong the administration.⁹

§ 1936. Bids Both in Bulk and Parcels with Acceptance of Greater Aggregate.—The bids may be taken both in bulk and in parcels, and the greater aggregate be accepted.

§ 1937. Trustee's Judgment Ordinarily of Controlling Weight in Fixing Details, but Creditors, and Even Bankrupt, Heard.—As to whether the sale shall be public or private, in bulk or in parcels, and, in short, as to the details of time, manner and place of sale, etc., the trustee's judgment should ordinarily control;¹⁰ although undoubtedly, creditors are entitled to be heard as to the advisability of the different provisions of the proposed order of sale, and likewise the bankrupt, where his interests are measurably affected. But, in any event, the final determination rests with the court.¹¹

In *re Columbia Iron Wks.*, 14 A. B. R. 526, 142 Fed. 234 (D. C. Mich.): "This controversy and that relative to the question whether the property should be sold in bulk or in parcels, are matters for determination by the court and not by vote of creditors."

§ 1938. Ten Days Notice by Mail Requisite.—Ten days notice by mail must be given to all creditors who are scheduled and to all who have filed claims whether scheduled or not, of all proposed sales, whether at public auction or private sale;¹² except that the court may omit notice where the property is of a perishable nature.

As heretofore noted, one of the abuses in the administration of insolvent estates before the advent of the Bankruptcy Act was the slipping through of sales made in the interest of the debtor himself or of some favored

9. In one case the court refused to order a sale to a reorganized corporation which it was proposed to form but which would have given only its unsecured notes, of long time, therefore, especially since the current obligations of the new corporation were to have precedence and the future plans of the new corporation were indefinite and it was not fully clear that more could be realized by cash sale. In *re Cornell Co.*, 26 A. B. R. 252, 186 Fed. 859 (D. C. N. Y.). It might further be said, relative to the Cornell case, that the matter involved was, in any event, rather a composition than a sale.

10. See ante, § 898. In *re Columbia Iron Wks.*, 14 A. B. R. 526, 142 Fed.

234 (D. C. Mich.); In *re Zehner*, 27 A. B. R. 536, 193 Fed. 787 (D. C. La.).

11. In *re Zehner*, 27 A. B. R. 536, 193 Fed. 787 (D. C. La.).

12. Bankr. Act, § 58 (a): "Creditors shall have at least ten days notice by mail, to their respective addresses as they appear in the list of creditors of the bankrupt, or as afterwards filed with the papers in the case by the creditors, unless they waive notice in writing of (4) all proposed sales of property."

Allgair v. Fisher, 16 A. B. R. 281, 143 Fed. 962 (C. C. A. N. J.); In *re Monsarrat* (No. 2), 25 A. B. R. 820 (D. C. Hawaii); In *re Nevada-Utah Corp.*, 28 A. B. R. 409, 198 Fed. 497 (D. C. N. Y.).

creditor. An application usually could be filed and granted immediately without notice and the sale made forthwith; and the only remedy then left to the creditors was a fruitless effort to have the sale set aside for fraud or collusion—always difficult matters to prove. If creditors have notice of such sales, they can protect themselves; and the very fact that notice is given them operates to deter parties from attempting to rob the estate by secret and summary sales. Thus it is, that this requirement of notices to creditors of all proposed sales is one of the safeguards of the purity of bankruptcy administration.¹³

Compare, as to importance of notice to creditors in bankruptcy administration, *In re Kyte*, 26 A. B. R. 507, 189 Fed. 531 (D. C. Pa.): "All acts necessary to be done to accomplish the purpose of converting the assets of the estate and distributing the same to and amongst the creditors legally entitled thereto, as well as any act tending to increase the value of the estate, or in some material manner benefit the estate of the bankrupt, whereby the general interests of all creditors may be advanced, constitute the administration of the estate. The intent of the law is to administer the estate for the general interests of all the creditors with the least possible expense, and to this end when any proposition of interest, as well as detrimental to the creditors is made, the law provides that all the creditors shall have notice of a time and place to meet and either assent to or disapprove of such proposition. This undoubtedly is a provision of the law which has been created to throw a safeguard around the interests of the creditors so that the opportunity for abuse or mismanagement of their interests may be reduced to a minimum."

And a sale made after the time set in the notice has expired, will be set aside.

Allgair v. Fisher, 16 A. B. R. 281, 143 Fed. 962 (C. C. A. N. J.): "The orders of the referee of December 24, 1904, and March 11, 1905, had practically expired by the failure of the trustees to make sale of the property, pursuant to the terms thereof, either at private or public sale, and their inability to make sale thereunder was disclosed, and the public sale had been adjourned without day; I think the referee's power in the matter was for the time ex-

¹³. But see *In re Hawkins*, 11 A. B. R. 48 (D. C. N. Y.), where the court seems to assume that the referee has discretion as to whether notice to creditors need be given at all. This can not be correct law. Perhaps that was a case of perishable property after all and the statement of facts merely fails to show it.

Also see *In re Knox Automobile Co.*, 32 A. B. R. 67, 210 Fed. 569 (D. C. Mass.), where the court following *In re Hawkins* dispensed with notice to creditors because the court felt that the trustee intended to use every reasonable effort to get the highest possible price for the property and that he would be in a better position if not hampered by formal orders as to what to do. Surely the court in the face of the express provision in the statute for

notice to creditors should not be allowed to substitute its opinion as to the best manner of conducting sales, especially on such slim grounds. This is but another instance of the growing tendency in the bankruptcy courts to disregard the statutory provisions for notices to creditors which form such an important safeguard against collusive sales and improper dispositions of the assets. The tendency in state legislation,—notably the recently enacted assignment law of New York—is to lay stress on notices to creditors; so, also, in the Bankruptcy Act itself, whose provisions all point to such notices; and the tendency of the bankruptcy court to annul these provisions by judicial construction or simply by ignoring them is to be deplored. Compare, § 1944.

hausted, and that he should then have given a new notice to the creditors and lienors. I deem such notice not only proper, but essential, under the circumstances, and hence that the orders dated May 24, 1905, June 1, 1905, and June 15, 1905, were unwarranted, and should be set aside."

Needless to say, the regulation only applies to sales by officers of the bankruptcy court, and does not apply to sales by pledgees and others in possession of securities given by the bankrupt. Such securities may be sold in accordance with the terms of the agreement of pledge; thus, as to securities where the pledgee is given the right to sell without notice;¹⁴ and this is so even though the receiver or trustee acts for the pledgees in making the sale and proceeds under an order of the bankruptcy court in so doing.¹⁵

§ 1939. Public Auction of Real Estate.—Where real estate is to be sold at public auction, the U. S. equity rules provide that in equity cases there must be at least four weeks advertisement, once a week, and that the sale be made either at the county courthouse or on the premises.¹⁶

So far as sales by the trustee are concerned, they are not to be considered as controlled by the Act of March, 1893, whether the sale be of real estate or personal property, or be by public auction or private sale, for the trustee, by operation of law, has the title of the property as owner.¹⁷

Robertson v. Howard, 229 U. S. 254, 30 A. B. R. 611: "We come then to consider whether the court of bankruptcy in Illinois, in the proceedings to sell the certificates and the interest in the land evidenced by them, was required to conform to the provisions of the act of Congress of March 3, 1893, chap. 225, heretofore referred to. * * * We think this question must be answered in the negative. It is not to be doubted that the subject of bankruptcy was special in its nature, and that in enacting the Bankruptcy Act it was proposed

14. In *re Carothers & Co.*, 27 A. B. R. 921, 193 Fed. 687 (D. C. Pa.).

15. In *re Carothers & Co.*, 27 A. B. R. 921, 193 Fed. 687 (D. C. Pa.).

16. See 27 U. S. Stat. at L., ch. 225, §§ 1, 2, 3, p. 751, approved Mch. 3, 1893: "Sec. 1. That all real estate or any interest in land sold under any order or decree of any United States court shall be sold at public sale at the court house door of the county, parish, or city in which the property, or the greater part thereof, is located, or upon the premises, as the court rendering such order or decree of sale may direct.

"Sec. 2. That all personal property sold under any order or decree of any court of the United States shall be sold as provided in the first section of this act, unless, in the opinion of the court rendering such order or decree, it would be best to sell it in some other manner.

"Sec. 3. That hereafter no sale of real estate under any order, judgment,

or decree of any United States court shall be had without previous publication of notices of such proposed sale being ordered and had once a week for at least four weeks prior to such sale in at least one newspaper printed, regularly issued and having a general circulation in the county and state where the real estate proposed to be sold is situated, if such there be. If said property shall be situated in more than one county or state, such notice shall be published in such of the counties where said property is situated as the court may direct. Said notice shall, among other things, describe the real estate to be sold. The court may, in its discretion, direct the publication of the notice of sale herein provided for to be made in such other papers as may seem proper."

17. In *re Edes*, 14 A. B. R. 382, 135 Fed. 595 (D. C. Me.); In *re National, etc.*, Co., 27 A. B. R. 92, 193 Fed. 232 (D. C. Mass.).

comprehensively to deal with the subjects coming within the scope of bankruptcy legislation, which included, of course, the authority of courts of bankruptcy to deal with the sale of the real and personal estate of a bankrupt.

* * * This provision makes it manifest that it was the purpose of Congress to give bankruptcy courts full and complete equitable power in matters of the administration and sale of the bankrupt estate, wholly irrespective of the mere situs of the property, the controlling factor being, not where the property is situated, but did it pass to the trustee, and is it a part of the estate subject to administration under the direction of the court. In view of the fact that the bankruptcy law was enacted long after the passage of the statute of 1893, and of the complete right of administration which the Bankruptcy Act confers over the property, real and personal, of the bankrupt estate, we think it follows that the authority to realize, by way of sale, on the property of the bankrupt estate, cannot be held to be limited by the provisions of the act of 1893. Indeed, this conclusion is additionally demonstrated by the fact that, as recognized by No. 18 of the general orders in bankruptcy, in disposing by sale of the property of the bankrupt, a bankruptcy court, as to both real and personal property, may, if reason for so doing exists, direct a private sale to be made. We do not stop to refer to the many cases in the lower Federal courts which have applied and enforced the view which we here maintain, as we think it unnecessary to do so."

In *re La France Copper Co.*, 30 A. B. R. 381, 205 Fed. 207 (D. C. Mont.): "The main contention is based on noncompliance with Act March 3, 1893, ch. 225, 27 Stat. 751 (U. S. Comp. St. 1901, p. 710). It will be observed said act antedates the Bankruptcy Act, and is one of restriction upon jurisdiction. The Bankruptcy Act confers full and exclusive jurisdiction, both legal and equitable, to administer bankrupt estates. In so far as it is not express, it authorizes the Supreme Court to prescribe procedure. It would seem to provide a complete system and the only rule for such administration. Act March 3, 1893, seems to relate to judicial sales pursuant to some order or decree creating or declaring a right to sell, and which right could not be exercised, but for the order or decree; sales necessarily authorized and ordered by the court; sales void, but for such order or decree; sales divesting the title of the former owner. Sales in bankruptcy are not like these in character. The Bankruptcy Act operates as a transfer from the bankrupt to the trustee of the title to the bankrupt's property. The trustee's duty is to collect and reduce to money the property of the estate. To that end he has the usual powers and discretion of trustees for like purposes, save to the extent restricted by the Bankruptcy Act. The latter act places no restrictions on the trustee's sale of realty at public auction and requires no order of the court therefor. The Supreme Court, however, by general orders, prescribes authorization by the court before any private sale shall be made. Even this is but a restriction on power otherwise possessed by the trustee. Though the trustee reduces the estate to money, 'under the direction of the court,' this no more necessitates an order of the court to sell realty at public auction than to collect a chose in action. Therein the court may, but need not, give special directions, in the nature of orders. The creditors are entitled to notice of proposed sales, but this may be given by the trustee by order of the judge. * * * It would seem clear that a trustee in bankruptcy has power to sell outright realty of the estate without any order of court, and after such notice and at such place as in his judgment seems best for the estate. The fact that in the instant case an order of sale was made by the court (referee) does not affect the legal aspect. To procure the order is discreet, and it might in some contingencies protect

the trustee; but it is not necessary, and it neither adds to nor detracts from his otherwise power and discretion. No doubt the court can control the trustee and any abuse of his discretion, order sales, and dictate the procedure; but here, as in equity, the trustee may without special order do that which the court might order. For the reasons given, I am persuaded Act March 3, 1893, has no application to sales in bankruptcy."

In *re Britannia Mining Co.*, 29 A. B. R. 472, 203 Fed. 45 (C. C. A. Wis.): "Undoubtedly the Act of March 3, 1893, applies not only to federal courts then in existence, but also to those subsequently created, unless something in the organic act exempts them; and governs as well any possible new forms of judicial sales under decrees as foreclosure, execution, and partition sales then known. But, in our judgment, the Act of 1893 has no application to trustees' sales of the assets of bankrupt estates for this prime reason; in a judicial sale under order or decree, the order or decree fixes the relative rights of the parties in the property according to the status or conduct or contract between them, and the sale itself is the thing that divests all the parties of their title and confers it upon another; while in a trustee's sale the sale itself is not the thing that divests the parties in interest of their title; there is no order or decree of the bankruptcy court that gives the creditors any adjudicated rights in specific property—the statute gives them the right to a distribution after the assets, not already in money, have been reduced to money; there is no order or decree that divests the bankrupt of his title—the only decree against him is the adjudication of bankruptcy, and after that he still has the legal title (in trust for the trustee thereafter to be elected); when the trustee is elected, *eo instanti* he is vested, not by virtue of any order or decree of court, but 'by operation of law' (§ 70a), with the title of the bankrupt as of the date of adjudication. In short, the statute operates as a self-executing conveyance from the bankrupt to the trustee. His quality of title is the same as if the statute, instead of operating directly, had required that the courts should either cause the bankrupt to convey to the trustee or should appoint a commissioner to execute a conveyance in the bankrupt's name. So when the trustee, as grantor, conveys what he acquired as grantee, he is not making a sale within the purview of the Act of March 3, 1893. If he needs to resort to the ancillary jurisdiction of bankruptcy courts in other districts (which jurisdiction, independently of the amendment in 1910 of sec. 2, subd. 20, was held to exist, *Babbit v. Dutcher*, 216 U. S. 102, 23 A. B. R. 519, 30 Sup. Ct. 372, 54 L. Ed. 402, 17 Am. Cas. 969), it is not for the purpose of becoming vested with title and the right and power to sell and convey, but only to aid him in acquiring or holding or delivering possession.

"Other sections of the Bankruptcy Act and of the General Orders, hereinabove quoted, only restrict, in the interest of the beneficiaries of the trust, the manner in which the trustee shall exercise his otherwise unlimited power of disposition; and they confirm us in the conclusion we have derived from a consideration of the nature of the trustee's title, namely, that Congress in the Bankruptcy Act has provided a comprehensive and exclusive method of administering estates of bankrupts."

§ 1940. Private Sales, Real Estate or Personal Property, Advertised and Conducted as Court Directs.—Private sales, both of real estate and personal property, may be made in such manner as the court may direct.

An unauthorized private sale vests no title in the purchaser.¹⁸

18. In *re Monsarrat* (No. 1), 25 A. B. R. 815 (D. C. Hawaii).

Although there is no law requiring the fixing of an upset price, the better practice is, before granting an order to sell at private sale, to require the showing of an offer, actually tendered, sufficient to warrant the court in granting an order of private sale, and then to set in the order of sale a corresponding minimum price which should, of course, not be less than such offer.¹⁹

§ 1941. Who May File Petition to Sell: Trustee, Receiver, Marshal, Bankrupt.—It is absolutely necessary after the trustee's election that the petition to sell be filed by him, for he is the one vested with title, and all proceedings in behalf of the estate are to be taken in his name. Before the election of a trustee, it may be filed by the receiver or marshal, if the marshal be in charge, and perhaps by a creditor, or even by the bankrupt himself.²⁰

Instance, by receiver, *In re Becker*, 3 A. B. R. 412, 98 Fed. 407 (D. C. Pa.): "In the case now before the court the sale was made, not by a trustee, but by a receiver; and objection is raised to a receiver's power to sell the property of the bankrupt. The objection is based upon the language of clause 3 of § 2, which authorizes courts of bankruptcy to appoint receivers, 'for the preservation of estates, to take charge of the property of bankrupts after the filing of the petition, and until it is dismissed or the trustee qualified.' It is argued that this limits the power of receivers, and forbids them to do more than hold possession of the bankrupt's property during a certain interval. I do not think the argument is sound. The clause restricts the power of the court to appoint, confining it to cases of absolute necessity, and then goes on to state the purpose for which the appointment may be originally made. But, after a receiver has once gone into possession, it may become necessary to sell the property for the very purpose of preserving it, or its value—which is, of course, the essential matter—either in whole or in part. In such event, I think the court has ample power to order or confirm a sale, either under the power to preserve, implied by clause 3 itself, or under clause 7 of the same section, which empowers the court to 'cause the assets of bankrupts to be collected, reduced to money and distributed.'"

As long as creditors have ten days notice by mail, especially if the final deed or bill of sale is made by the trustee, it would seem enough.²¹

19. Compare, however, post, §§ 1949, 1956.

Fixing Upset Price of Lease to Insure Payment of Rentals.—See, where an upset price was fixed in order that a lease might not be sold for less than what would insure the payment of rentals, *In re Gutman* (*Nelson v. Denmark*), 28 A. B. R. 643, 197 Fed. 472 (D. C. Ga.).

20. Compare, as to perishable property, Rule XVIII (3). Instance, *Sale by receiver*, *In re Vogt*, 20 A. B. R. 457, 159 Fed. 317, 163 Fed. 551 (D. C. N. Y.); *In re Duke & Son*, 28 A. B. R. 195, 199 Fed. 199 (D. C. Ga.).

Sale Not by Trustee but by Commissioners.—In one case, on ordering a

sale clear and free of liens the court ordered the sale to be made by commissioners under direct order of the judge rather than by the trustee under the referee's order and this manner of sale was approved in that instance. *Sturgiss v. Corbin*, 15 A. B. R. 543, 141 Fed. 1 (C. C. A. W. Va.).

See "Sales before Adjudication," § 1943.

21. Inferentially, *In re Fisher Co.*, 14 A. B. R. 366, 135 Fed. 223 (D. C. N. J.).

Effect of Pendency of Composition Proceedings on Right to Sell.—And the pendency of composition proceedings, does not divest the jurisdiction to sell, although, unless composition proceedings are being delayed unduly,

It has apparently been assumed, in some cases, that it is not even necessary that the trustee take any part in the sale.²²

§ 1942. Perishable Property May Be Sold without Notice.—But perishable property may be sold without notice to creditors, if the court so orders.²³

Obiter, *In re Edes*, 14 A. B. R. 382, 135 Fed. 595 (D. C. Me.): "While this General Order has no force as legislation, and while it is not even a judicial interpretation of the statute, it is an order of the Supreme Court of the United States, based upon the bankruptcy statute. It cannot be held to be in derogation of such statute. Under its provisions a perishable estate may be sold, even without notice to the creditors, and the courts have been very liberal in their construction of what is 'perishable.' The Federal courts have in fact liberally interpreted the whole statute, as giving full equitable powers to the court. For instance, although § 58 provides that creditors shall have notice of all proposed sales of property, still, under the general powers and discretion given by the court in § 70b, it is the custom to order sales of perishable personal property even without notice."

§ 1943. Sales before Adjudication.—As a rule, no order of sale should be made until after adjudication, unless the property be of such nature that a sale is necessary to preserve its value.²⁴

undoubtedly jurisdiction to sell is suspended. *In re Fisher & Co.*, 14 A. B. R. 366, 135 Fed. 223 (D. C. N. J.): "The first objection, namely, that a petition for composition is now pending, is not valid. It is true that an effort to effect a composition with the creditors of the bankrupt has been made, but the money necessary to pay taxes and other debts or demands having priority required to be deposited by § 12b of Bankruptcy Act, has not been deposited, though several months have intervened since the court declared that such deposit must be made before any composition could be confirmed."

Sale Where Trustee's Election Set Aside and New Election Ordered.—Probably it would not affect the validity of an intervening sale that the election of the trustee is set aside and a new election ordered. Compare, *In re Evening Standard Pub. Co.*, 21 A. B. R. 156, 164 Fed. 517 (D. C. N. Y.).

22. *Instance, In re Vogt*, 20 A. B. R. 243, 457, 159 Fed. 317, 163 Fed. 551 (D. C. N. Y.).

23. Rule XVIII (3), Gen. Orders in Bankruptcy: "Upon petition by a bankrupt, creditor, receiver, or trustee, setting forth that a part or the whole of the bankrupt's estate is perishable, the nature and location of such perishable estate, and that there will be loss if the same is not sold immediately, the court, if satisfied of the facts stated and that the sale is required in the in-

terest of the estate, may order the same to be sold, with or without notice to the creditors, and the proceeds to be deposited in court."

Form of Petition to Sell Perishable Assets.—The Supreme Court's form No. 46 is the prescribed form for a petition to sell perishable assets. The petition should show the following facts; it should describe the property; state its nature and location; allege that it is perishable and that there will be loss if the same is not sold immediately.

Impliedly (though the court speaks of "private" sale as if it were synonymous with sale without notice to creditors. Manifestly there may be a private sale, i. e. a sale without notice to bidders, and yet notice to creditors, who are the beneficiaries, be given). *In re Pedlow*, 31 A. B. R. 761, 209 Fed. 841 (C. C. A. N. Y.).

24. *In re Kelly Dry Goods Co.*, 4 A. B. R. 528, 102 Fed. 747 (D. C. Wis.); *In re Harris*, 19 A. B. R. 635 (D. C. Ala.); *In re Desrochers*, 25 A. B. R. 703, 183 Fed. 991 (D. C. N. Y.); *Instance of sale, In re Duke & Son*, 28 A. B. R. 195, 199 Fed. 199 (D. C. Ga.); *Instance, In re B. D. Garner & Co.*, 18 A. B. R. 733, 153 Fed. 914 (D. C. Ala.); *Instance, In re Peerless Finishing Co.*, 28 A. B. R. 429, 199 Fed. 350 (D. C. N. Y.); *Instance of sale, In re Garner & Co.*, 18 A. B. R. 733, 153 Fed. 914 (D. C. Ala.).

The reason is obvious; before adjudication it cannot be certainly known that the property belongs to the creditors. Moreover, until the appointment and qualification of a trustee there is no officer having title to the property in behalf of creditors.²⁵ These reasons are particularly cogent in attempted sales of real estate before adjudication. Only by the bankrupt's consent, and doubtfully then, will good title pass to the purchaser. And even in such instances the ten days notice should go to all creditors unless the property also be perishable.²⁶

§ 1944. Meaning of "Perishability."—"Perishability," under the Act of 1898, would seem to refer to physical deterioration, more than to financial depreciation through the goods becoming unseasonable, although the decisions are not uniform in this regard.²⁷

In *re Beutel's Sons Co.*, 7 A. B. R. 768 (Ref. Ohio): "The question is thus presented: May a stock of goods not physically nor intrinsically perishable, be sold without notice to creditors as perishable property under the Bankruptcy Act of 1898. The old law of 1867 provided in § 5065 as follows: 'When it appears to the satisfaction of the court that the estate of the debtor or a part thereof is of a perishable nature, or liable to deteriorate in value, the court may order the same to be sold in such manner as may be deemed most expedient under the direction of the messenger or assignee, as the case may be, who shall hold the funds received in place of the estate disposed of.'

"No provision existed under the old law requiring notices to creditors of sales except in cases of public sales, and then only by advertisement in the newspapers.

"On the other hand, no provision is found in the present act permitting the sale of any assets as perishable, but the statute does specifically provide in § 58 (4) that 'Creditors shall have at least ten days' notice by mail to their respective addresses as they appear in the list of creditors of the bankrupt, or as afterwards filed with the papers in the case by the creditors, unless they waive notice in writing of—(4) all proposed sales of property.'

"The Supreme Court, however, has in rule XVIII (3) attempted to make an exception to this requirement of notice in all cases of sales and has laid down the following order: 'Upon petition by a bankrupt, creditor, receiver or trustee, setting forth that a part of the whole of the bankrupt's estate is perishable, the nature and location of such perishable estate, and that there will be loss if the same is not sold immediately, the court, if satisfied of the facts stated and that the sale is required in the interest of the estate may order the same to be sold, with or without notice to the creditors, and the proceeds to be deposited in court.'

"Congress, in passing the present act, had constantly before it the provisions of the old act, and also the experience of litigants under it; and it must be assumed, as indeed the rules of statutory construction oblige us to assume, that where we find changes in the present act in regard to the same subject

²⁵. But compare, *In re Maloney*, 21 A. B. R. 502 (Sup. Ct. D. of C.), quoted at § 1950; also, compare, ante, § 386½.

²⁶. But where a sale has been ordered by the referee in the absence of the judge, before adjudication, it will not be set aside where a fair sum has been realized and there is no evidence

of injurious effect upon any interests. *In re Kelly Dry Goods Co.*, 4 A. B. R. 528, 102 Fed. 747 (D. C. Wis.).

See ante, § 386½; also compare, *In re Fulton*, 18 A. B. R. 591, 153 Fed. 664 (D. C. N. Y.), quoted at § 386½.

²⁷. Compare, ante, §§ 386, 564.

matter such changes are to be considered as indicating a distinct change in the minds of the lawmakers. Where, therefore, we find the present act providing for ten days' notice to creditors of all proposed sales without exception, we would naturally assume that Congress was unwilling to have any sales made without notice. Whatever force and effect the Supreme Court's general order No. 18 has we must be careful at any rate to extend it no further than its strict wording permits, and at any rate not to give it such an effect as to practically restore the practice of the old law of 1867, which Congress has thus strongly disapproved.

"Now note the working of the old law of 1867. It provides where the property 'is of a perishable nature or liable to deteriorate in value.' Evidently a distinction exists between property that is of a perishable nature and that which is simply liable to deteriorate in value. The first refers to that which has intrinsic, physical perishability—something that will decay or die or shrink or shrivel, change in its physical nature, whilst the latter is much broader, covering that which depreciates in value from whatever cause, unseasonableness, poor market, expense, etc.

"The Supreme Court's order XVIII under the present law, however, speaks only of 'perishable property' and does not attempt to engraft an exception upon the clear cut words of the statute in favor of property which is liable merely to deteriorate in value.

"No doubt the careful framers of the present act bore in mind the scandals possible where entire estates could be disposed of without notice, to interested parties under the easy term that it is property liable to deteriorate in value."

But the Circuit Court of Appeals of the Second Circuit has expressly held to the contrary of the author's view, and has held a stock of handkerchiefs a month before Christmas to be perishable, although the purchaser, himself a private auctioneer, later on held a public auction thereof on notice and advertisement, disposing of the stock at a profit.

In *re Pedlow*, 31 A. B. R. 761, 209 Fed. 841 (C. C. A. N. Y.): "General Order No. 18 permits the court, in its discretion, to sell perishable property at private sale and it seems to us that this provision must include property which is liable to deteriorate in value and price, as well as property which deteriorates physically. Unquestionably a cargo of bananas would be perishable, but assume that we are dealing with a cargo of rifles for which belligerents will pay an increased price if immediate delivery can be made, but which will be practically valueless if delivery be delayed. It seems to us that 'perishable' fairly construed, means property which, for any reason, will deteriorate in value and that what is and what is not perishable may be safely left to the discretion of the court."

Compare, In *re Harris*, 19 A. B. R. 635, 156 Fed. 875 (D. C. Ala.): "But I further stated in that case that this was confined only to such cases in which it was clear to the court that the property was, in fact, perishable in part or in its entirety, or would greatly deteriorate if held without a sale, and only that portion which was of such nature could be ordered sold."

In *re Milne Mfg. Co.*, 21 A. B. R. 468 (Ref. N. Y.): "Real estate may be considered perishable within the meaning and intent of General Order 18, when it consists of buildings, rapidly deteriorating and in a dilapidating condition and requiring immediate expenditure of a large sum of money by the trustee to prevent absolute loss. An order to sell perishable property, even real estate, rests in the sound discretion of the court, and where it is not affirmatively shown that gross injustice has been done to

the creditors, a sale of such property at private sale, by the trustee, will not be disturbed for lack of notice to a creditor of the application for an order to sell or for confirmation of the sale. Where a building, used as a manufacturing plant by an involuntary bankrupt, was rapidly deteriorating in value and was unsalable, and an offer was made therefor of a sum representing its fair value, which offer was conditioned upon conveyance being made within a shorter period of time than would allow notice to be given in accordance with the usual practice in sales of bankrupt properties, and where great loss would be occasioned by failure to make the sale, the court is justified in making an order, allowing the trustee to consummate the sale without notice, and a sale so made will not be set aside."

The author submits that the case *In re Pedlow* announces dangerous doctrine. The Bankruptcy Act is largely a mere statutory regulation of the procedure in the administration of insolvent estates, prescribing the method found by years of experience best suited to secure honesty and efficiency in this most important field. Where creditors, the real owners of the assets and beneficiaries of the trust, are notified of sales there is to a certain extent an additional check and guaranty against collusive and improper disposition of the assets. The tendency in the more recent legislation on insolvency matters, both state and national, is unquestionably towards an insistence upon notices to creditors. Indeed, it is manifest that Congress, the law-making body, by providing in § 58 of the Act for notices to creditors as to not less than nine or ten of the most important steps in the practical administration of the assets, the "business" part of the administration, so to speak, intended creditors to be kept in close touch with the practical side of insolvency administration and above all with the manner, time and place of the disposition of the assets. It is significant that Congress in the present act specifically requires these notices, particularly of "all sales," unequivocally and unambiguously, whilst the old law was silent on the subject, and left such matters of notice to the absolute discretion of the court without even indicating the desirability of any notice. The present Act was framed largely from our experience under the old Act, and such change indicates a distinct and positive intention that creditors, under the present act, should have notices without fail and without evasion. To be sure, the Supreme Court has provided by its Rule XVIII for sales of "perishable property," but such rule should be construed to aid the legislative intent, not to thwart it, particularly not to directly contradict its plain and salutary provisions. It should be confined to as narrow boundaries as possible, rather than be stretched to its utmost limits. "Perishability" by common acceptance, as also in all attachment and execution law, refers solely to physical decay. No one would think of a stock of handkerchiefs as "perishable," nor could they be sold by an attaching officer as "perishable."^{27a}

^{27a}. There was no finding indeed, by the lower court in the case criticised, that the goods were "perishable," but merely that they would become "unseasonable."

The logical result of the ruling is a reversion to the practice under the old law of 1867, whose evils the framers of the present law strove earnestly to obviate. However that may be, the decision practically means that, in the Second Circuit at any rate, no notices need be given to creditors in any case where the court deems at the time a better price may be obtained by sale without notice.

§ 1945. Referee to Order Sale after Reference.—After reference to the referee, the referee is the court for the purpose of granting the order to sell.²⁸

§ 1946. Before Adjudication Judge Alone to Order Sale, unless Unable to Act.—Before adjudication orders to sell may be made only by the judge;²⁹ except, of course, that in the absence or disability of the judge, the referee may act, upon receipt of a certificate from the district clerk of the judge's absence or disability.³⁰

§ 1947. To Be at Public Auction, unless Expressly Authorized at Private Sale.—Sales must be at public auction, unless expressly authorized at private sale.³¹ And, as noted ante, § 1936, the bids may be taken in bulk and in parcels, and the greatest aggregate offer be accepted.

§ 1948. For Good Cause Shown May Be at Private Sale.—Upon application to the court, and for good cause shown, the trustee may be authorized to sell any specified portion of the bankrupt's estate at private sale.³²

In re Edes, 14 A. B. R. 382, 135 Fed. 595 (D. C. Me.): "There can be no question but that a bankruptcy court, under the broad powers given by the Bankruptcy Law, may order a sale of either real or personal property at private sale."

28. Official Forms 42, 43, 44, 45 and 46; *In re Styer*, 3 A. B. R. 424, 98 Fed. 290 (D. C. Pa.); *In re Fisher & Co.*, 14 A. B. R. 368, 135 Fed. 223 (D. C. N. J.); *In re Nevada-Utah Corp.*, 28 A. B. R. 409.

Journal Entry of Order to Sell Perishable Assets.—His order should read somewhat as follows: "Upon this — day of —, 19—, the trustee's (or receiver's or bankrupt's) petition for leave to sell perishable property came on for hearing without notice to creditors at which hearing no adverse interest was represented (see Gen. Order No. XXIII) (or, if the case be so, after hearing adverse interests) and it appearing to the satisfaction of the court (for the court must be 'satisfied') that the allegations of said petition are true and that the property therein described is perishable in its nature and the loss will result if it be not sold immediately and that the sale thereof is required in the interest of the estate and that no-

tice thereof should be omitted, now it is ordered that said petition be and it hereby is granted and said trustee is directed to sell said property at public sale forthwith for not less than three-fourths its appraised value and without notice to creditors and to deposit the proceeds thereof in the court to await the further orders of the court."

29. *In re Styer*, 3 A. B. R. 424, 98 Fed. 290 (D. C. Pa.); *In re Peerless Finishing Co.*, 28 A. B. R. 429, 199 Fed. 350 (D. C. N. Y.).

30. *In re Kelly Dry Goods Co.*, 4 A. B. R. 528, 102 Fed. 747 (D. C. Wis.).

31. See Supreme Court's General Order No. XVIII (1) and (2): "All sales shall be by public auction unless otherwise ordered by the court." *In re Nevada-Utah Corp.*, 28 A. B. R. 409, 198 Fed. 497 (D. C. N. Y.).

32. Gen. Order 18 (2). Instance, *In re Nevada-Utah Smelting Corp.*, 29 A. B. R. 754, 202 Fed. 126 (C. C. N. Y.).

And the discretion of the referee in ordering a private sale will not be interfered with, except for plain abuse.³³ Real estate may be so sold as well as personal property.³⁴ Notices should be sent to the creditors of a proposed private sale equally as in cases of proposed public sales, "private sales" meaning merely that a public offering of the property to bidders, come who may, is dispensed with.^{34a}

In cases of private sale, the trustee must keep an accurate account of each article sold, and the price received therefor and to whom sold; which account he shall file at once with the referee.³⁵

Jurisdiction to compel the purchaser to complete his contract of sale exists the same in private sales as in public auctions.³⁶

§ 1949. Sale Subject to Approval and to Be for Seventy-Five Per Cent.—Both the real and the personal property shall, when practicable, be sold subject to the approval of the court; it shall not be sold otherwise than subject to the approval of the court for less than seventy-five per centum of its appraised value.³⁷

But the appraisal is not so binding that a sale for less than seventy-five per cent will not pass good title, if, in the sound discretion of the court, the price is adequate.^{37a}

And an upset price need not be fixed in the order of sale, since the statute itself expressly provides that the property shall not be sold, unless subject to the approval of the court, for less than seventy-five per cent.³⁸

However, in practice, before granting an order to sell at private sale, it should be shown to the court that an actual offer at a certain price has been made, sufficient to warrant the court in granting an order of private sale; in which event, the order granted should, in proper practice, set a minimum price.

It is not necessary that the creditors should have notice of an application for the confirmation of the sale, if they have previously been given notice of the proposed sale itself.³⁹

33. *In re Hawkins*, 11 A. B. R. 49, 125 Fed. 633 (D. C. N. Y.): The court in this case seems to labor under the misapprehension that notice can be dispensed with at the referee's discretion. Such discretion does not exist except in cases of perishable property. See, also, *In re Knox Automobile Co.*, 32 A. B. R. 67, 210 Fed. 569 (D. C. Mass.).

34. *In re Edes*, 14 A. B. R. 382, 135 Fed. 595 (D. C. Me.).

34a. For discussion as to what amounts to a "public sale," see *In re Nevada-Utah Smelting Corp.*, 29 A. B. R. 754, 202 Fed. 126 (C. C. A. N. Y., overruling *S. C.*, 28 A. B. R. 409, on this point, the court holding that an advertisement addressed to "creditors, stockholders and

other parties in interest" is not broad enough to include an invitation to the general public and hence can not be considered as a public sale).

35. Gen. Ord. 18 (2).

36. *In re Jungmann*, 26 A. B. R. 401, 186 Fed. 302 (C. C. A. N. Y.).

37. Bankr. Act, § 70 (b); *In re Metallic, etc., Co.*, 27 A. B. R. 408, 193 Fed. 300 (D. C. Pa.); *In re La France Copper Co.*, 30 A. B. R. 381, 205 Fed. 207 (D. C. Mont.).

37a. See ante, § 1924.

38. *Schuler v. Hassinger*, 24 A. B. R. 184, 177 Fed. 119 (C. C. A. Ala.).

39. *In re Nevada-Utah, etc., Corp.*, 28 A. B. R. 409, 198 Fed. 497 (D. C. N. Y.).

§ 1950. Trustee's Sale, a Judicial Sale.—A trustee's sale in bankruptcy is a judicial sale in distinction from an execution sale.

A judicial sale is a sale of particular property in the custody of the court, specifically pointed out by the court and ordered during the pendency of proceedings concerning it; while an execution sale is a sale of whatever property belonging to the execution debtor the sheriff can seize. In judicial sales, such as are sales by trustees in bankruptcy, the court is the real seller and the trustee is its agent to obtain the highest bid—the sale is not consummated nor does title pass until confirmation. By the act of confirmation, the sale becomes complete and the title passes. In execution sales, on the other hand, the court simply has rendered a judgment for money and is then done with the matter. The sheriff is the real seller and title passes at once to the highest bidder. A result of this distinction is that, in execution sales, the purchaser immediately becomes invested with rights which can only be divested by showing that he himself, or his agent, has been guilty of fraud; while in judicial sales, such as trustee's sales in bankruptcy, until confirmation, the so-called purchaser has no such rights, has no title at all—he is simply a preferred bidder waiting for the court to accept his offer,⁴⁰ and is subject to the general rules and principles of procedure relating to other judicial sales, excepting in so far as the bankruptcy act is in conflict therewith;⁴¹ and the court may refuse to accept his offer on much weaker grounds than would be required to set aside a sale on execution, where title has already passed.

In *re Harvey*, -10 A. B. R. 567, 568, 122 Fed. 745 (D. C. Pa.): "In the case under consideration, the trustee sold at public sale certain real estate of the bankrupt, upon which the city held several liens for municipal taxes. The sale was without previous authority from the court, but it was duly confirmed and the confirmation was equivalent to a prior order. I do not doubt that this was a judicial sale. 17 Am. & Eng. Encycl. Law, 954, 955."

In *re Maloney*, 21 A. B. R. 502 (Sup. Ct. D. of C.): "Another objection is, that the sale was made by the receivers, when the title was in the trustee, relating back to the date of the adjudication in bankruptcy; and that therefore the receiver could convey no title. This argument is fallacious in this, that the sale is not made by the receivers, but is a sale made by the court; and whether the sale is brought about by the efforts of the receivers and their petition to the court, or by the direction of a trustee, or other officer, the title is under the control of the court; and if it should be necessary in order to perfect the title, the court could at any time require the trustee to join the sales, or in a conveyance to the purchaser."

Inferentially, In *re Shea*, 11 A. B. R. 211, 126 Fed. 153 (C. C. A. Mass.): "But on a true construction of § 70 (b) the case before us is not one of set-

40. In *re Groves*, 2 N. B. N. & R. 31 (Ref. Ohio); inferentially, In *re Ethier*, 9 A. B. R. 160, 118 Fed. 107 (D. C. Wis.); contra, *Steadman v. Taylor*, 1 N. B. N. 283; In *re Monsarrat* (No. 1), 25 A. B. R. 815 (D. C. Hawaii); In *re Metallic Specialty Mfg. Co.*, 27 A. B. R. 408, 193 Fed. 300 (D. C. Pa.);

Camden v. Mahew, 129 U. S. 73; (*Coal City*) *House Furnishing Co. v. Hogue*, 28 A. B. R. 258, 197 Fed. 1 (C. C. A. W. Va.).

41. *Coal City, etc., Co. v. Hogue*, 28 A. B. R. 258, 197 Fed. 1 (C. C. A. W. Va.).

ting aside a sale, but of affirming it. * * * so that, strictly speaking, we are within the rule of *Williamson v. Berry*, 8 How. 495, 546, 12 L. Ed. 1170, to the effect that, when a sale is made subject to confirmation, no title vests until it is confirmed."

And it is just as much a judicial sale where the court simply approves an offer made as where it first orders a sale and thereafter approves an offer.⁴²

§ 1951. And Court Has Greater Discretion than in Other Sales.

—Being a judicial sale, the court may refuse to accept bids and may set aside sales on lesser grounds than in other sales.⁴³

Inferentially, *Pewabic Min. Co. v. Mason*, 149 U. S. 356: "It may be stated generally that there is a measure of discretion in a court of equity, both as to the manner and conditions of such a sale, as well as to ordering or refusing a resale."

§ 1952. "Gross Inadequacy" Sufficient to Refuse Confirmation.

—Therefore, mere gross inadequacy of price, in bankruptcy, without more, is sufficient to prevent confirmation of a trustee's sale.⁴⁴

Obiter, *In re Belden*, 9 A. B. R. 679, 120 Fed. 524 (D. C. N. Y.): "This court does not doubt its power to open this sale on the ground of inadequacy of consideration, but to do that, in face of the opposition of all the creditors interested in that consideration, would be unjustifiable."

Inferentially, but obiter, *In re Ethier*, 9 A. B. R. 160, 118 Fed. 107 (D. C. Wis.): "The object of the sale in question, under order of the court, was to obtain the best price for the stock of goods, through open and unrestricted bidding; and a judicial sale so made will not be set aside except for gross inadequacy of price, or for circumstances impeaching the fairness of the sale."

Obiter, *In re Shapiro*, 19 A. B. R. 125, 154 Fed. 673 (D. C. Pa.): "That a sale of this kind may be set aside upon the sole ground of inadequacy is sustained by *Ballentyne v. Smith*, 205 U. S. 285; but in order that this should be so the difference between what the property has brought and its real value must be such as to be unconscionable."

§ 1953. But Mere Inadequacy, or Merely a Better Offer, Insuffi-

cient.—But mere inadequacy of price, unless it amounts to gross inade-

42. *In re Jungmann*, 26 A. B. R. 401, 186 Fed. 303 (C. C. A. N. Y.).

43. Also, see cases cited ante and post, §§ 1950 and 1952.

May Disregard Official Appraisal Made by the Duly Appointed Appraisers.—The court may, if it deems the price adequate, wholly disregard the official appraisal. *In re Zehner*, 27 A. B. R. 536, 193 Fed. 787 (D. C. La.).

44. *In re Groves*, 2 N. B. N. & R. 31 (Ref. Ohio).

Evidence of true value: Price obtained by the purchaser, on resale of the purchased goods, shortly thereafter, has been held incompetent. *Sebring v.*

Wellington, 6 A. B. R. 671, 63 N. Y. App. Div. 499. But see strong dissenting opinion. Compare also, *In re Bloch*, 6 A. B. R. 300, 109 Fed. 790 (C. C. A. N. Y.).

Instance held not gross inadequacy of price, *Schuler v. Hassinger*, 24 A. B. R. 184, 177 Fed. 119 (C. C. A. Ala.).

Inferentially, *In re Foster*, 25 A. B. R. 96, 181 Fed. 703 (D. C. Vt.), quoted at § 1971; inferentially, *In re Monsarrat* (No. 2), 25 A. B. R. 820 (D. C. Hawaii). Compare *In re Knosher & Co.*, 28 A. B. R. 747, 197 Fed. 136 (C. C. A. Wash.).

quacy, is not sufficient ground for setting aside a sale, unless there be additional circumstances.⁴⁵

Graffam v. Burgess, 117 U. S. 191: "In this country, Lord Eldon's views were adopted at an early day by the courts, and the rule has become almost universal that a sale will not be set aside for inadequacy of price, unless the inadequacy be so great as to shock the conscience or unless there be additional circumstances against its fairness; being very much the rule that has always prevailed in England as to setting aside sales after the master's report has been confirmed."

Sturgis v. Corbin, 15 A. B. R. 546 (C. C. A. W. Va.): "A sale made under a judicial decree will not, when no misunderstanding existed among the bidders, and when no fraud is shown, be set aside for mere inadequacy of price, unless such inadequacy is so gross as fairly to raise a presumption of fraud. The practice of opening biddings and of setting aside sales made during the progress of judicial proceedings should not be encouraged, as it is not conducive to the interests of litigants, and it tends to shake public confidence in the validity and finality of judicial sales, and to unduly prolong litigation. A purchaser at a judicial sale, who has complied with the terms thereof, or who shows his willingness and ability so to do, is not only entitled to the protection of the court, but as a party to the proceeding, made such by his purchase, is so situated as to be entitled to the court's decree of confirmation, in the absence of the inadequacy, fraud, or mistake before alluded to."

In re Shapiro, 19 A. B. R. 125, 154 Fed. 673 (D. C. Pa.): "The stock of the bankrupt was appraised at \$5,000, and was sold at a public sale by the trustee for \$2,800. It is now asked that a resale be ordered, the creditors who make the request having agreed to bid at least \$3,200. That a sale of this kind may be set aside upon the sole ground of inadequacy is sustained by *Ballentyne v. Smith*, 205 U. S. 285; but in order that this should be so the difference between what the property has brought and its real value must be such as to be unconscionable. * * * The advance which is offered, however, is inconsiderable—only \$400—and is not enough to warrant the court in overturning what has been done after this interval. There is also a condition attached that the stock shall be the same as when it was inspected by the representative of creditors, which further detracts from it. It is suggested that notice of the sale was not received by some of the creditors and that the party who had been sent to attend it missed his train. But however this might help to induce the court to order a resale if properly substantiated, the controlling thing as the case stands is that the amount guaranteed is too small to bother with. This may favor the bankrupt, who is said to be the real purchaser—his brother having the name of it—at the expense of his creditors, who also, as it seems, have other and older grievances against him, two previous failures and a fire standing to his credit. But however this may be, they will have to get satisfaction some other way, the matter here not warranting further controversy."

And merely a better offer, however beneficial to creditors, will not suffice to set aside the sale, unless misconduct existed in the sale amounting to imposition and fraud.⁴⁶

⁴⁵. *In re Metallic, etc., Co.*, 27 A. B. R. 408, 193 Fed. 300 (D. C. Pa.); *In re National, etc., Co.*, 27 A. B. R. 92, 193 Fed. 232 (D. C. Mass.); *In re Knosher & Co.*, 28 A. B. R. 747, 197 Fed. 137 (C.

C. A. Wash.); instance, *In re Kronrot*, 25 A. B. R. 738, 183 Fed. 653 (D. C. N. Y.).

⁴⁶. Impliedly, *In re Belden*, 9 A. B. R. 679, 120 Fed. 524 (D. C. N. Y.).

In *re Ethier*, 9 A. B. R. 161, 118 Fed. 108 (D. C. Wis.): "The fact of a better offer subsequent to the sale, however beneficial to the creditors, will not furnish ground to disturb the transaction, after confirmation, without misconduct in the sale amounting to imposition and fraud."

Sturgis v. Corbin, 15 A. B. R. 547 (C. C. A. W. Va.): "The advance offer of \$7800 [4 per cent. increase] was, of itself, under the circumstances attending the purchase by *Sturgis*, not sufficient to warrant the setting aside of the sale."

And merely a prospective better bidder, although himself a creditor, where neither the other creditors nor the bankrupt are asking for it, but, on the contrary, are objecting, cannot have a sale set aside, even though offering a better bid.⁴⁷ Confirmation will not be refused for inadequacy of price where the sale was regularly and fairly made, where the objecting party is a creditor who was present and was a bidder at the sale, even though at the time of objecting he offers to bid slightly more.⁴⁸

§ 1954. Stifling of Competition; Misconduct of Trustee or Unfairness to Bidders.—Much more is the stifling of competition or misconduct of the trustee sufficient ground for refusing confirmation.⁴⁹

In *re Shea*, 11 A. B. R. 210, 126 Fed. 153 (C. C. A. Mass., affirming 10 A. B. R. 481): "In passing, we may add that the exercise of discretion to set aside a sale would be justly called for so long as parties intending to bid had seasonably advised the officer conducting the sale that they so intended, and were prevented from bidding without fault on their part. Under such circumstances, whether the loss of the opportunity to bid happened through inadvertence on the part of the officer conducting the sale, or through his intention, or by any accident for which the intending bidders were not responsible, would be immaterial."

Thus, where a trustee sold the bankrupt's equity at private sale, without giving notice thereof to an intending bidder according to promise, the equity being worth three times the sum the trustee expected to receive, the court set aside the sale upon the intending bidder filing an agreement to

47. In *re Belden*, 9 A. B. R. 679, 120 Fed. 524 (D. C. N. Y.).

48. In *re Thompson*, 2 A. B. R. 216 (Ref. Pa.).

49. In *re Ethier*, 9 A. B. R. 160, 118 Fed. 107 (D. C. Wis.), the facts in which case are peculiar: Intending purchasers had agreed among themselves to make one bid, the highest, each. Another apparent purchaser was really agent of one of them and bid it in. Had the remaining purchasers known the facts they would have continued to bid.

In *re Groves*, 2 N. B. N. & R. 31 (Ref. Ohio).

In *re Hawley*, 9 A. B. R. 61, 117 Fed. 364 (D. C. Iowa), in which case the trustee purchased at his own sale but was allowed for the money expended

by him for betterments on the land as well as for the purchase price.

Reimbursement and Attorney's Fees to Creditor Succeeding in Getting Sale Set Aside for Collusion.—A creditor who has succeeded in getting a collusive sale by the trustee set aside and thereby eventually a greater fund has been brought into the court may be allowed reimbursement of expenses including attorney's fees incurred, such allowance not being by virtue of § 64 (b) (2) but under the general equity powers of the court. In *re Groves*, 2 N. B. N. & R. 466 (Ref. Ohio); also, compare (merely suggestively and analogously, however), *obiter*, In *re Road-armour*, 24 A. B. R. 49, 177 Fed. 379 (C. C. A. Ohio).

pay three times as much for the equity at the next sale.⁵⁰

Participation of the purchaser in the misconduct need not be proved.⁵¹ And unfairness towards bidders may warrant refusal of confirmation.⁵²

Sturgis v. Corbin, 15 A. B. R. 547, 141 Fed. 1 (C. C. A. W. Va.): "The advance in the bid, it thus appears, was less than 4 per cent. on the sum at which it had been sold to Sturgis. The acceptance of this belated bid, was, we think, under the circumstances attending said sale, a mistake. This offer was made by a party interested in the proceeds of the sale, one who was thoroughly familiar with all the incidents connected with it, who was well advised as to the value of the property, and who had himself been an unsuccessful bidder during one of the times at which the property had been offered for sale. There is an entire absence of fraud; in fact no intimation of its existence is made. It is not shown that any mistake or misunderstanding existed among the bidders concerning the property itself, or the terms under which the sale was made. The additional offer was not of such a character as would demonstrate inadequacy of price, or justify a refusal to confirm. If a judicial sale has been fairly conducted, as was the sale we now consider, the rights of the purchaser should be protected, not only because it is his due, but also for the purpose of protecting such sales from the evil and chilling influences of instability and doubt."

But the fact that the highest bidder is acting for another whose identity he refuses to disclose, does not warrant the trustee in refusing to accept the bid, especially where, on being informed that his offer would be refused, the bidder agrees to become personally responsible.⁵³

And that the attorney of the ultimate purchaser at an auction sale of a bankrupt's property by the trustee had a private arrangement with the auctioneer that the bid of any other person should be raised \$50 each time

⁵⁰ *In re Shea*, 11 A. B. R. 207, 126 Fed. 153 (C. C. A. Mass.).

Where a sale of the bankrupt's equity for its appraised value is set aside upon the petitioner filing an agreement to bid three times as much, the omission from the record upon a revisory petition, praying an affirmance of the sale, of any specific finding that the value of the equity exceeded the amount which it brought at the sale, is not material, it being assumed that the court acted rightly and found that the value of the equity was triple the price the trustee was to receive therefor. *In re Shea*, 11 A. B. R. 207, 126 Fed. 153 (C. C. A. Mass.).

⁵¹ *In re Shea*, 11 A. B. R. 207, 126 Fed. 153 (C. C. A. Mass.); impliedly, *In re Belden*, 9 A. B. R. 679, 120 Fed. 524 (D. C. N. Y.); [1867] *In re O'Fallon*, Fed. Cases 10,445; *In re Groves*, 2 N. B. N. & R. 30 (Ref. Ohio).

⁵² *In re Shea*, 11 A. B. R. 207, 126 Fed. 153 (C. C. A. Mass.).

But compare facts in *In re Mitchell*, 15 A. B. R. 739 (Ref. Mass.), where the

court confirmed a private sale to the bankrupt who waited until all bids were in and then offered a slightly higher bid; the court, however, refusing still higher offers from creditors afterwards. Such a sale was manifestly unfair to the bona fide bidders.

But, where intending bidders had access to the inspection of a will in which the bankrupt had a certain interest, the fact that they did not appreciate the legal effect of certain ambiguous provisions therein which might render the estate more valuable than was supposed, and which the other bidders had had explained on the bankrupt's examination does not constitute misrepresentation warranting the refusal of the confirmation of the sale. *In re Crouse*, 28 A. B. R. 540, 196 Fed. 907 (D. C. N. Y.).

(Coal City) House Furnishing Co. v. Hogue, 28 A. B. R. 258, 197 Fed. 1 (C. C. A. W. Va.).

⁵³ *Coal City, etc., Co. v. Hogue*, 28 A. B. R. 258, 197 Fed. 1 (C. C. A. W. Va.).

until a sign was given by the attorney to stop, does not render the sale invalid or prevent its confirmation.

In *re Ketterer Mfg. Co.*, 19 A. B. R. 638, 156 Fed. 719 (D. C. Pa.): "The complaint, with regard to this, is that it was a discouragement to other bidders to have their bids immediately overtopped by this amount by the auctioneer, without there being any apparent bid by anyone present, conveying the impression that the auctioneer was simply puffing the sale. But I see no occasion for setting the sale aside upon that ground. There was nothing underhanded or unfair in the arrangement referred to, nor was it indeed out of the ordinary, according to the way in which auction sales are conducted. A bid may be, and often is, conveyed by a mere nod, which no one but the auctioneer sees or understands, this course being taken for the very purpose of keeping it from being known who the bidder is, who, without this, might have the property run up upon him by puffers, beyond what he otherwise would be compelled to give. It is not required, as argued, that there should be an open and obvious bidder, whom other competitors can see and know, at the time. It is sufficient, if all parties desiring to bid have a fair chance, the announcement by the auctioneer, from time to time, of the amount bid disclosing to each just how the sale is going, and bids in good faith, from responsible parties, alone being entertained."

And that the purchaser is allowed to apply upon the purchase price securities held upon the bankrupt's property, is not an unfairness invalidating the sale.⁵⁴

Schuler v. Hassinger, 24 A. B. R. 184, 177 Fed. 119 (C. C. A. Ala.): "The fourth proposition, that the terms of sale were unequal and unfair, and competition was thereby stifled, is based upon the fact that the purchaser was permitted by the terms of the order of sale to turn in, in payment of the price, admitted securities; the argument being that the holders of securities could buy without paying cash while an outsider would be compelled to pay cash. * * * The contention in this case seems to disregard the general rule which prevails in all foreclosure and execution sales wherein it is not deemed proper and necessary to require purchasers to put up cash with one hand to take it down with the other."

§ 1954½. Injury to Innocent Parties, Avoidance of Confusion, etc.—The court will not refuse to confirm a sale where such refusal would create confusion and, perhaps, injury to innocent persons; and this is especially true where those attacking the sale may just as effectively have their grievances litigated in other courts.

In *re Pittsburg, etc., Co.*, 28 A. B. R. 613, 197 Fed. 106 (D. C. N. Y.): "The attacking creditor Revelas is a mining engineer, and was the supervising manager of the bankrupt's property at the time of the adjudication and for several years prior thereto. He claims that the bankrupt owes him \$8,601.85. He was

54. Similarly, where the trustee is not ordered to sell, but merely to solicit bids, the order providing for the filing of objections to bids, upon objections being filed and the bidding being reopened on the hearing, one whose bid had previously been the

highest will not be heard to complain either of the rejection of his bid or of the sale to a subsequent higher bidder, especially where he refused to bid upon the reopening of the bids. In *re Chandler*, 28 A. B. R. 89, 194 Fed. 944 (C. C. A. Ill.).

on the ground and knew that the company was in a bad way. (Letters of October 1, 1910; October 14, 1910; October 30, 1910; December 24, 1910; March 29, 1911.) How much would he have bid at the sale? He insists that Nessler and the rest were in a conspiracy to defraud him, and he points to Nessler's telegram of April 16, 1911. In that telegram Nessler distinctly stated that the receiver was without funds, that great efforts would be made to reorganize, and that, in such event, Nessler would make 'every effort to protect' his interest. Nessler, in the same telegram, urged Revelas not to leave under any circumstances, and to be patient. Revelas construes this as evidence of a scheme to keep him away from New York, the scene of the bankruptcy proceedings, but I regard this as a natural course under the circumstances. Obviously Nessler and his associates wanted the one man familiar with conditions to stay at the property, while efforts were being made to save something from the wreck. The receiver communicated with Revelas, asking how much money would be required to retain his services. He was advised by Revelas that he required practically immediately a sum which the receiver could not possibly pay, and thereupon Revelas left Nome, went to Dick Creek, but had no further dealings with the receiver or the officers of the bankrupt. In the fall of 1911 Revelas came to New York, and it is claimed that Nessler, who now was secretary and treasurer of the Inspiration Gold Mining Company, offered Revelas an opportunity to invest \$500, the same as the principal stockholders had done, that being the largest sum accepted from anybody, and extended this opening to come in with the rest, but Revelas refused so to do. If this is so, then Nessler carried out the promise of his telegram of April 16, 1911, to look out for Revelas in the reorganization. Revelas, however, was not satisfied and later began this proceeding. Meanwhile new rights have sprung up, new money has been ventured, and the project looks more hopeful. To order a resale now will create endless confusion, and may deprive those who have engaged in the enterprise of the legitimate fruits of their investment.

"On the other hand, if Revelas has been injured, he has been damaged only to the extent of his claim of some \$8,600. If he is the victim of a conspiracy, the courts are open to him, and, in an action at law or in equity (as he may be advised, he may unmask the scheme of which he complains, if such existed, and obtain his just due. In such an action all the parties in interest will have their day in court, which, in this proceeding, they have not. Many details of the testimony, and referred to by the special master, though considered, are not here discussed, but in the final analysis the true test is not what the situation is now, but what it was on June 25, 1911, when the order of sale was made. With the property embarrassed by vexatious complications, heavily in debt and requiring new capital, where was the creditor or outside investor willing to risk much on a bankrupt mining venture in far-off Alaska?

"The motion is denied, and the report of the special master is confirmed. Submit order on two day's notice."

§ 1955. Bankrupt May Be Bidder.—The bankrupt may be a bidder.⁵⁵

55. In re Mitcheli, 15 A. B. R. 739 (Ref. Mass.); Clark v. Clark, 17 How. 315; In re Kingman, 5 A. B. R. 251 (Ref. Mass.); Holbrook v. Coney, 25 Ills. 543; [1867] Pheips v. McDonald, 2 McArthur 375; contra, Marsh v. Heaton, 1 Low 278; In re Nat'l Mining Exploration Co., 27 A. B. R. 92, 193 Fed. 232 (D. C. Mass.).

It has been held in one case that a bankrupt repurchasing from the purchaser at the trustee's sale his own claim against a person, can not thereafter enforce his claim against an undisclosed principal not named as debtor. Shesler v. Patton, 17 A. B. R. 372, 114 App. Div. 846.

§ 1955¼. **But Referee, Receiver Nor Trustee, etc., Not.**—But neither the referee,⁵⁶ receiver nor trustee may be a purchaser.⁵⁷ The prohibition is not confined to those officers, however, nor does it depend upon a contract of employment, nor upon some formal relation of trust or confidence—the disability grows out of a duty, and embraces all persons who have a duty to perform with respect to the property of others and with the proper performance of whose duty the character of purchaser of such property may be in any degree inconsistent.⁵⁸

Thus, an agent of a receiver or trustee (or, in one case it has been held even one obtaining confidential information from a receiver or trustee) may not be a purchaser;⁵⁹ nor may an appraiser be a purchaser.⁶⁰

In *re Frazin & Oppenheim*, 24 A. B. R. 598, 181 Fed. 307 (C. C. A. N. Y.): "It is a long established principle of equity jurisprudence that a trustee cannot become a purchaser of the trust estate. And not only trustees, strictly speaking, but agents, attorneys and all persons acting in behalf of other persons and obtaining confidential information concerning their affairs cannot purchase their property except under certain restraints not necessary to be considered here. Lord St. Leonards thus stated these elementary principles in his treatise on Vendors and Purchasers (*Sugden on Vend. and Purch.*, 2d Am. Ed., from 5th London Ed., p. 422) and his statement has many times been quoted with approval by judges and text writers: 'It may be laid down as a general proposition that trustees, unless they are nominally so, as trustees to preserve contingent remainders, agents, commissioners of bankrupts, assignees of bankrupts, solicitors to the commission, auctioneers, creditors who have been consulted as to the mode of sale or any person who, by their connection with any other person or by being employed or concerned in his affairs, have acquired a knowledge of his property, are incapable of purchasing such property themselves, except under the restrictions which will shortly be mentioned. For if persons having a confidential character were permitted to avail themselves of any knowledge acquired in that capacity they might be induced to conceal their information and not to exercise it for the benefit of the persons relying upon their integrity. The characters are inconsistent. *Emptor emit quam minimo potest, venditor vendit quam maximo potest.*'

"The application of these principles is not dependent upon the engagement of one person by another in a confidential capacity. There need be no contract of employment at all. There need be no formal relation of trust. The disability grows out of the duty. In our opinion the rule of equity should be so broadly applied as to embrace all persons who have a duty to perform with respect to the property of others and with the proper performance of whose duty the character of purchaser of such property may be in any degree inconsistent.

"In *King v. Remington*, 36 Minn. 15, 26, the Supreme Court of Minnesota said: 'Nor is the application of the rule confined to a particular class of persons, as guardians, solicitors, attorneys, etc. It applies universally to all who come

56. Bankr. Act, § 39 (b) (3): "Referee shall not * * * (3) purchase, directly or indirectly, any property of an estate in bankruptcy."

57. In *re Hawley*, 9 A. B. R. 61, 117 Fed. 364 (D. C. Iowa); In *re Mitchell*, 15 A. B. R. 739 (Ref. Mass.).

58. In *re Frazin & Oppenheim*, 24 A.

B. R. 598, 181 Fed. 307 (C. C. A. N. Y.), quoted *supra*.

59. In *re Frazin & Oppenheim*, 24 A. B. R. 598, 181 Fed. 307 (C. C. A. N. Y.), quoted *supra*.

60. In *re Frazin & Oppenheim*, 24 A. B. R. 598, 181 Fed. 307 (C. C. A. N. Y.), quoted *supra*.

within its principle, which principle is that no party can be permitted to purchase an interest in property and hold it for his own benefit where he has a duty to perform in relation to such property which is inconsistent with the character of a purchaser on his own account and for his individual use.'

"But there are other considerations underlying these equitable principles where the question is presented whether an officer of a court who has duties to perform with respect to property in the custody of the court can buy it for his own benefit. These are considerations of public policy. And no consideration of public policy is deeper grounded upon fundamental principles—upon principles which reach the very foundations of judicial authority—than that courts and court officers must be disinterested in the management of estates committed to their charge. It cannot be permitted that officers appointed by courts to perform duties regarding property in custody of the law should speculate therein. It cannot be permitted that court officials should use their official positions for personal profit. The question is not one of fraud or good faith, of gain or loss to the estate, in a particular instance. The rule goes far deeper than that. It is applicable in every case in order to secure and maintain the impartial administration of justice.

"Upon no courts is the obligation to enforce these principles of public policy greater than upon the courts of bankruptcy of the United States. The object of Congress in enacting the bankruptcy laws was to secure the efficient and fair administration of estates. The one thing, more than all others, which creditors and bankrupt alike have the right to expect from those having official duties to perform relating to the property of the estate."

That the price paid was adequate is immaterial.

In *re Frazin & Oppenheim*, 24 A. B. R. 598, 181 Fed. 307 (C. C. A. N. Y.): "Nor is it of importance whether the price paid at the sale was adequate. As already indicated, the application of the rules of equity and consideration of public policy which we have examined is not dependent upon the question of fairness or unfairness in price."

It may be improper for an appraiser, even after appraisal filed, to be a purchaser.

Obiter, In *re Frazin & Oppenheim*, 24 A. B. R. 598, 181 Fed. 307 (C. C. A. N. Y.): "Whether an appraiser after filing his report might be regarded as so far *functus officio* that he could become the purchaser of the property of the estate, need not be determined here. For manifest reasons there would be less objection to such a purchase than to one made while the duties of the appraiser were uncompleted. On the other hand, it may be that the underlying principles of public policy go so far as to disable an official appraiser from purchasing from the estate at any time property which he has valued."

However, it was held in one case that the sale was not invalidated because the bid had been made by attorneys who had been employed also by the trustee from time to time, no retainer nor permanent employment by either the trustee or the purchaser having been shown and the attorneys having no connection with the trustee in the sale.⁶¹ And the prohibition ought not to be distorted into a refusal to give information asked for in good faith by prospective purchasers provided others are not denied equal opportunity.

61. In *re National, etc., Co.*, 27 A. B. R. 92, 193 Fed. 232 (D. C. Mass.).

§ 1955¹/₂. Reorganization Committees, etc., as Purchasers.—

The mere fact that the purchaser is a reorganization committee or a reorganized corporation, is not, in and of itself, proof of an improper sale; in fact, such method may become the only adequate method of taking care of a large plant with diversified interests.⁶²

Schuler v. Hassinger, 24 A. B. R. 184, 177 Fed. 119 (C. C. A. Ala.): "The second proposition, that the sale was collusive, is based upon the fact that prior to the sale there was a reorganization committee for the purpose of purchasing the property in bulk; that the trustees favored such reorganization; and that the order of sale permitted the trustees to receive, as part of the purchase price, admitted securities constituting liens upon the property. That there should be a reorganization agreement for the purpose of buying in the property of the bankrupt corporation cannot be objected to. In fact, it furnishes the only way that a large diversified property and plant like that of the Southern Steel Company can be sold and purchased without disastrous results to creditors and stockholders, and the creditors have every right to organize themselves for the purpose of protecting their interests. These are propositions that need neither argument nor authority to support. That the trustees should in good faith encourage and approve a plan which looked to the successful settlement and winding up of the bankruptcy estate, and which met the approval of creditors and had the consent of all classes interested, was perfectly proper. See *Cook on Corporations*, Vol. 3, p. 3189; *Platt v. Philadelphia R. R.* (C. C.), 65 Fed. 872. The reorganization agreement set forth in the record as approved by the trustees provided for the mortgage and lien holders and the unsecured creditors and all stockholders, both common and preferred; and it was assented to by all of the first mortgage bondholders, 99³/₄ per cent. of the collateral trust note holders, 86 per cent. of the proved claims, 87 per cent. of the preferred stockholders, and 90 per cent. of the common stockholders. Such a reorganization agreement seems so fair on its face that the court itself could well have approved it if brought before it in proper way; in fact, it seems to have all of the elements of a composition which is favorably provided for in the bankruptcy law."

However, the bankruptcy court will not order a sale of all the assets, against the objection of minority creditors, to a reorganized corporation which it is proposed to form and which, it is proposed, will give only its own unsecured obligations therefor, especially when it does not appear how the reorganized corporation is to raise the funds nor in what manner it will carry on business, nor, for that matter, whether more could not be derived from a cash sale.⁶³

§ 1955³/₄. Selling Rights of Action.—While the bare right of action to set aside a fraudulent transfer may not be sold, yet the trustee may sell

⁶². In *re National, etc., Co.*, 27 A. B. R. 92, 193 Fed. 232 (D. C. Mass.). Instance, In *re Pittsburgh Dick Creek Mining Co.*, 28 A. B. R. 613, 197 Fed. 106 (D. C. N. Y.).

Compare, reorganization and sale of assets before bankruptcy, done to hinder and delay creditors. In *re Medina*

Quarry Co., 24 A. B. R. 769, 179 Fed. 929 (D. C. N. Y.).

Compare criticism in *In re E. T. Kenney Co.*, 14 A. B. R. 611, 136 Fed. 451 (D. C. Ind.).

⁶³. In *re Cornell Co.*, 26 A. B. R. 252, 186 Fed. 859 (D. C. N. Y.).

property and with it the right to set aside a fraudulent transfer thereof:

In re Downing, 27 A. B. R. 309, 192 Fed. 683 (D. C. N. Y.): "It seems to me that inasmuch as the trustee in bankruptcy is vested with all the right, remedies and powers of a judgment creditor of the bankrupt with execution returned unsatisfied, and one of those rights is (assuming the transfer was in fraud of creditors) to set aside the transfer, have the specific real property sold, or sell same, and the proceeds applied to the payment of all proved and allowed claims against the bankrupt, the trustee has an interest in such property. His rights and interest are something more than a mere possibility or expectancy, not coupled with an interest in or growing out of property. And it is something more than a litigious right. If the action is prosecuted successfully the judgment reaches and operates on the specific property sold or transferred by the bankrupt—the title of the fraudulent vendee is divested—and the true title transferred to a purchaser as to the trustee in bankruptcy and the proceeds so far as necessary go to the trustee for creditors or to the purchaser of such rights from such trustee. It is true that the transferee (assignee) of the trustee in bankruptcy would not be prosecuting the action for the benefit of the creditors of the bankrupt but in his own interest and for his own benefit. The answer to this is that such assignee of the trustee has paid a consideration for the transfer of the rights to the trustee, who holds the same for the creditors. The creditors do not object to this mode of realizing on the claim or right of action, but in fact make a resort thereto necessary."

§ 1956. May Accept Bid of Less than Seventy-Five Per Cent.—The court may accept a bid of less than seventy-five per cent of the appraised value, without ordering a reappraisal.⁶⁴ Nevertheless, the appraisal should not be disregarded. In some jurisdictions by local rule, the court will not approve a sale at less than two-thirds, although it will, of course, order reappraisal if good ground therefor exists.

It is not necessary that the order fix an upset price, since the statute provides that the assets shall not be sold otherwise than subject to the approval of the court for less than seventy-five per centum of the appraised value.⁶⁵

§ 1957. Inherent Power to Refuse Confirmation or to Set Aside, Even Where Not Expressly Ordered "Subject to Approval."—The inherent power of the court to disapprove and set aside an improper sale made under its order is not taken away by this provision of § 70 (b) of the act, even where the sale is not made subject to its approval.

In re Shea, 10 A. B. R. 481, 122 Fed. 742 (D. C. Mass.): "Section 70 (b) * * * provides that, when practicable, property shall be sold subject to the approval of the court. The order to sell made by the referee in the case at bar contained no such limitation, and so the authority of the court to set aside

64. Impliedly, Bankr. Act, § 70 (b): "It shall not be sold otherwise than subject to the approval of the court for less than 75 per cent of its appraised value." Instance, In re Nevada-Utah Smelting Corp., 29 A. B. R. 754, 202 Fed. 126 (C. C. A. N. Y.); In re Zehner,

27 A. B. R. 536, 193 Fed. 787 (D. C. La.).

65. Schuler v. Hassinger, 24 A. B. R. 184, 177 Fed. 119 (C. C. A. Ala.). Compare, however, better practice, ante, §§ 1940, 1949.

this sale must depend upon that general authority to deal with sales made under its orders which is inherent in a court of bankruptcy. This authority is not, I think, taken away by the provision just cited."

In *re Shea*, 11 A. B. R. 210, 126 Fed. 153 (C. C. A. Mass., affirming 10 A. B. R. 481): "But on a true construction of § 70b the case before us is not one of setting aside a sale, but of affirming it. As we have already said, this provision has no such interpretation as that given it by the petitioner. So far from that, it clearly provides that in every case the sale shall be subject to the approval of the court when practicable, and even the limitation 'when practicable' does not apply when the sale is less than 75 per centum of the appraised value. In other words, under all circumstances the sale is subject to approval by the court 'when practicable;' and there is no question in this case that it was practicable to obtain such approval. Therefore the question is one of confirming and not of setting aside; so that, strictly speaking, we are within the rule of *Williamson v. Berry*, 8 How. 495, 546, 12 L. Ed. 1170, to the effect that, when a sale is made subject to confirmation, no title vests until it is confirmed."

But if a lesser bid is presented for approval, the burden of proof rests on the trustee recommending the confirmation, to show that it is proper to accept a bid of less than seventy-five per cent.⁶⁶

And a sale for less than seventy-five per cent conveys no title, unless confirmed by the court.⁶⁷

In *re Shea*, 11 A. B. R. 207, 126 Fed. 153 (C. C. A.): "If a judicial tribunal authorized to make a judicial sale expressly reserves the right to approve or disapprove, it certainly would require a very extreme case to justify some other tribunal in injecting its own discretion. The condition seems to be the same where the right to approve or disapprove is expressly reserved by statute."

Proceedings to set aside an improper sale by the trustee properly may be brought before the referee, but they may also be brought directly before the judge, General Order No. XII being directory only.

In *re Monsarrat* (No. 1), 25 A. B. R. 815 (D. C. Hawaii): "It therefore appears that this court is free to construe that part of General Order XII referred to and particularly the word 'shall' in the last sentence quoted, 'Shall be had before the referee.' There would not seem to be any reason to apprehend that the Supreme Court of the United States, in adopting this rule, had any intention of construing the Bankruptcy Act with the strict meaning contended for. Is it not more likely that the word 'shall' and the sentence in which it is found was used in a directory sense and that it was merely intended to mean that after reference the referee should have general charge of the subsequent proceedings, mainly having in view the administration of the ordinary progress of the settlement of the estate and the conduct of hearings therefor, according to the powers given him by the Bankruptcy Act, General Orders and rules of court? While he has these powers and duties, it does not appear that they are not also held by the judge. A District Court of a Territory is a court of bankruptcy and 'may include the referee.' Bankruptcy Act, § 1, divisions 7 and 8. Such court has original jurisdiction, among other powers, to allow and disallow claims, to cause the estates of bankrupts to be collected, reduced to money, and distributed, and

⁶⁶. In *re Groves*, 2 N. B. N. & R. 31 (Ref. Ohio).

⁶⁷. Bankr. Act, § 70 (b).

to determine controversies in relation thereto, 'except as otherwise provided in the Act Id. Sec. 2. The referee may perform 'such part of the duties * * * as are by this Act conferred on courts of bankruptcy and as shall be prescribed by rules or orders of the court of bankruptcy of their respective districts;' with some exceptions stated in the Act. Id. § 38, div. 4.

"While the referee is given these powers there are no words taking them away from the judge, who, as the court of bankruptcy is invested with original jurisdiction to do these things.

"This continuing jurisdiction of the judge appears to be recognized in practice, there being numerous cases of petitions to the District Courts, both in the nature of summary and plenary actions, and the trial of such actions by such courts, when it must be supposed that orders of reference has been made. *Whitney v. Wenman*, 198 U. S. 539, 14 A. B. R. 45, is one case in point. * * *

"The second ground of demurrer, i. e., that the petition presents an issue that can only be tried in a court of equity, must also be overruled; inasmuch as the court had possession of the shares of stock in the Palolo Land & Improvement Company, Limited, and the sale of them by the trustee being made without their appraisal, as required by law (Bankruptcy Act, § 70b), and at private sale without the order of the court (Gen. Order 18 div. 1), and not having been approved by the court, no title has vested in the grantee."

§ 1957¹. Purchaser Entitled to Hearing.—On an application to set aside the sale the purchaser is entitled to be heard to the extent of showing his rights in the premises, and to point out why the application should be denied.

In *re Kronrot*, 25 A. B. R. 738, 183 Fed. 653 (D. C. N. Y.): "A third party (who had the right to rely upon an absolute compliance with the terms of sale, and upon the absolute fairness of an auction conducted under the order of court) bid the property in, and while the sale was subject in all things to the confirmation of this court, that confirmation must depend upon the sufficiency of the notice, the compliance with all necessary or proper requirements in holding the sale, honesty and fair dealing in the action itself, and a proper treatment of the bidder in considering his rights after the property was knocked down to him, which would generally involve merely the possibility of his completing the purchase and of the adequacy of his bid; this last being particularly involved because of the provision of the statute that a bid of less than 75 per cent. cannot be completed, except upon confirmation thereof by the court."

§ 1958. Formal Approval Not Always Essential to Confirmation.—Formal approval is, perhaps, not always necessary to effect a confirmation.

In *re Shea*, 11 A. B. R. 211, 126 Fed. 153 (C. C. A. Mass.): "We do not undertake to say that § 70 (b) requires always a formal approval."

Thus, silent acquiescence in a sale for a considerable length of time may effect a confirmation;⁶⁸ or a crediting of the proceeds in the trustee's report or account, and a subsequent approval of the report or account by the court, may suffice to effect a confirmation.⁶⁹

68. *Obiter*, In *re Shea*, 11 A. B. R. 211, 126 Fed. 153 (C. C. A. Mass.).

69. In *re Shea*, 11 A. B. R. 211, 126 Fed. 153 (C. C. A. Mass.).

§ 1959. "**Caveat Emptor.**"—The rule of "caveat emptor" prevails in bankruptcy sales, as in all judicial sales, unless special direction otherwise is made in the order of sale.⁷⁰

And, a fortiori, is this true where the trustee states, at the sale, that he assumes no personal responsibility and does not warrant the property sold or its saleability.

In *re Frazin & Oppenheim*, 29 A. B. R. 212, 201 Fed. 86 (C. C. A. N. Y.): "To permit a purchaser, who thus speculates upon the value of the property bid in by him, to recover the price paid because subsequent events show that the interest purchased was less valuable than he supposed it to be, seems to us most inequitable. It would be difficult to imagine a clearer case for the application of the doctrine of caveat emptor. This buyer knew exactly what he was purchasing. From his point of view it was a wise purchase, it enabled his principals to make an advantageous arrangement whereby the old lease was cancelled and a new one made. In securing these advantages he put it out of his power to restore the trustee's interest in the old lease."

The sale, in the absence of special warranty by the trustee, conveys simply whatever interest the trustee possesses;⁷¹ but by special warranty, or representation, the trustee may be bound by a different rule. Whether he may, however, bind the estate thereby unless so authorized by the order of sale, is doubtful.

The referee may refuse to order the sale of a speculative claim, where

70. In *re Mulhauser Co.*, 10 A. B. R. 236, 121 Fed. 669 (C. C. A. Ohio); impliedly, *Owens v. Bruce*, 6 A. B. R. 322, 109 Fed. 72 (C. C. A. S. C.).

It is proper to refuse leave to persons who are not parties to the bankruptcy proceedings, to come in and assert rights in the property sold where they can assert their rights equally against the purchaser. In *re Mulhauser Co.*, 10 A. B. R. 236, 121 Fed. 669 (C. C. A. Ohio).

Trustee selling at "Invoice Price," where the actual purchase by the bankrupt originally had been made below invoice price. Purchaser, having full opportunity for examination refused reduction. *Owens v. Bruce*, 6 A. B. R. 322, 109 Fed. 72 (C. C. A. S. C.).

The rule of caveat emptor will not interfere with the court in its discretion setting aside a sale or granting a rebate of the purchase price where the defect is not a defect of the title or quality but merely a failure to get the quality of articles advertised as being sold. *Searchy v. McCourt*, 1 Fed. Rep. 261; 1 Md. 147; 3 La. Ann. 326. This rule would seem to be restricted to cases where the trustee could be put in statu quo and where the proportionate rebate is certain and ascertainable.

If the property has left the custody of the Bankruptcy Court that court will no longer protect one in his possession of it, not even though he be a purchaser from the trustee. *Briggs v. Stevens*, 7 Law Rep. 281.

The purchaser of the trustee's interests in property is entitled to maintain the same suits to set aside preferential or fraudulent transfers thereof or encumbrances thereon as the trustee himself would have been entitled to maintain. *Bryan v. Madden*, 15 A. B. R. 388, affirming 11 A. B. R. 763, 78 N. Y. Supp. 220. But compare, *Shesler v. Patton*, 17 A. B. R. 372, 114 App. Div. 846.

Purchaser of leasehold takes rights as he finds them, as to arrearage of rent, etc., In *re Ketterer Mfg. Co.*, 20 A. B. R. 694, 162 Fed. 583 (D. C. Pa.).

71. Instance, attempted sale of buildings separately from leasehold, where the landlord claims they are not severable, In *re Gorwood*, 15 A. B. R. 107 (D. C. Pa.). Impliedly, In *re Drumgoole*, 15 A. B. R. 261, 140 Fed. 208 (D. C. Pa.); Instance, purchase of a lease, title to which was in litigation. In *re Frazin & Oppenheim*, 29 A. B. R. 212, 301 Fed. 86 (C. C. A. N. Y.).

the sale is sought merely for the purpose of annoyance, and where the gain to the bankrupt estate will be merely nominal;⁷² but if anyone will give a substantial price for such claim, it is no duty of the trustee or court to refuse to sell.⁷³

A third party's rights may be asserted against the purchaser notwithstanding the trustee, in words, or by description, has attempted to sell such third party's goods, unless, of course, such third party has estopped himself by his conduct from asserting his rights.

In *re* *Bluestone Bros.*, 23 A. B. R. 264, 174 Fed. 53 (D. C. W. Va.): "But some doubt arises as to whether such jurisdiction could extend to the protection of the property after it has been sold and delivered to the purchaser. This question it becomes wholly unnecessary to decide in this case. It is only necessary to say that, in any event, the defendant, Devault, could only be stayed in his right to assert claim in a State court to the property under two conditions of things: First, in case there was conflicting claim to the property between himself and the bankrupt, which claim he had asserted in the bankruptcy court, and it had been there determined, or, being made a party to the proceeding, he had refused or failed there to assert his right, being called upon so to do; second, had by his fraudulent conduct at the time of sale, either by direct representation or by silent acquiescence, secured or allowed plaintiff to buy his goods, mingled with those of the bankrupts, as goods of the bankrupt properly to be sold."

§ 1960. Discretion in Approving or Setting Aside Sale Not to Be Revised, Except for Abuse.—The discretion of the court in approving or in setting aside the trustee's sale will not be revised, unless there has been an abuse of power, or the case is, in other respects, extreme.⁷⁴

In *re* *Shea*, 11 A. B. R. 207, 126 Fed. 153 (C. C. A. Mass.): "However all this may be, it should be remembered that, according to the practice in the Federal courts, an appellate tribunal is prohibited from revising the exercise of discretion in matters of this kind by a court having equitable jurisdiction, unless there is an abuse of power, or the case is in other respects extreme. There is nothing which this record properly brings to us, or even suggests, which justified the probability of the existence of an exception of that character."

Likewise in ordering a sale.⁷⁵

§ 1961. Resale.—Of course, after a sale has been set aside, a resale is to be ordered.⁷⁶

⁷². *Obiter*, In *re* *Gutterson*, 14 A. B. R. 495 (D. C. Mass.).

⁷³. In *re* *Gutterson*, 14 A. B. R. 495 136 Fed. 698 (D. C. Mass.).

⁷⁴. In *re* *Sanborn*, 3 A. B. R. 54, 96 Fed. 551 (D. C. Vt.).

Instance, where reviewing court refused to interfere, In *re* *Throckmorton*, 17 A. B. R. 856 (C. C. A. Ohio).

And review of an order setting aside a sale does not lie until a resale

has been ordered, made and confirmed. *Sturgis v. Corbin*, 15 A. B. R. 543, 141 Fed. 1 (C. C. A. Va.). Compare, In *re* *Metallic Specialty Mfg. Co.*, 27 A. B. R. 408, 193 Fed. 300 (D. C. Pa.).

⁷⁵. Impliedly, In *re* *Sanborn*, 3 A. B. R. 54, 96 Fed. 551 (D. C. Vt.): "What would be a proper case is a matter of discretion."

⁷⁶. Instance, reimbursement of first purchaser for intermediate outlays for

§ 1962. Summary Power to Compel Purchaser to Complete Sale.

—The bankruptcy court has summary power to compel a purchaser to complete his contract of sale.⁷⁷

In re Jungmann, 26 A. B. R. 401, 186 Fed. 302 (C. C. A. N. Y.): "By voluntarily becoming a purchaser of property sold under order of the court he submits himself to the jurisdiction of the court, and when such purchaser refuses without cause to carry out his contract he may be compelled to do so by rule or attachment issuing out of the court under whose decree the sale is had."

Mason v. Wolkowich, 17 A. B. R. 714, 150 Fed. 699 (C. C. A. Mass.): "Wherever a receiver, by direction of the court appointing him, makes a sale of assets in his possession, the parties concerned in the sale are bound to recognize him as an officer of the court; and consequently the court appointing the receiver, not only has power to enforce in a summary manner the completion of the contract of sale, but the parties involved are deemed to have consented to such a proceeding."

But the court, in accordance with the ordinary principles of equity, will relieve the purchaser where the contract was entered into through mistake.⁷⁸

And there is no sound distinction between a sale at auction and a private sale approved by the court so far as the purchaser's obligation to comply with his bid or offer is concerned.⁷⁹

§ 1962½. Plenary Action against Purchaser.—The trustee or receiver also has the right to institute plenary action against the purchaser.

Obiter, In re Jungmann, 26 A. B. R. 401, 186 Fed. 302 (C. C. A. N. Y.): "The receiver might, if he chose to do so, bring suit in a state court or in the circuit [now, District] court provided there was the requisite diversity of citizenship, alleging the making of the contract and asking damages for an alleged breach of it."

improvements. In re Fisher & Co., 17 A. B. R. 404, 148 Fed. 907 (D. C. N. J., affirmed sub nom. In re Wylie, 18 A. B. R. 503, 173 Fed. 281, C. C. A.). Instance (Coal City) House Furnishing Co. v. Hogue, 28 A. B. R. 258, 197 Fed. 1 (C. C. A. W. Va.).

⁷⁷. See post, § 1804.

Forfeiture of purchaser's deposit where public authorities refuse to transfer liquor license because of purchaser's personal unfitness, In re Comer & Co., 22 A. B. R. 558, 171 Fed. 261 (D. C. Pa.). But purchaser enti-

tled to return of deposit, when, In re Miller, 22 A. B. R. 560, 171 Fed. 263 (D. C. Pa.).

⁷⁸. In re [Maria F.] Caponigri, 32 A. B. R. 158, 210 Fed. 897 (C. C. A. N. Y.).

⁷⁹. In re Jungmann, 26 A. B. R. 401, 186 Fed. 302 (C. C. A. N. Y.).

Offer to pay "lowest market purchase price," whether accepted by order of court directing purchaser to pay "inventory prices made by official appraisers." In re Jungmann, 26 A. B. R. 401, 186 Fed. 302 (C. C. A. N. Y.).

CHAPTER XXXIX.

SELLING PROPERTY SUBJECT TO AND FREE FROM LIENS; AND TRANSFERRING RIGHTS TO PROCEEDS.

Synopsis of Chapter.

- § 1963. May Be Sold Subject to Liens.
- § 1964. If Not Mentioned to Be Otherwise, Sale Is Subject to Liens.
- § 1965. May Be Sold Free from Liens and Liens Transferred to Proceeds.
- § 1966. Lienholder's Consent Not Necessary.
- § 1967. Sale Clear and Free Ordered before Validity or Priority of Liens Determined.
- § 1968. But Not Where Lienholder Who Desires to Bid, Objects.
- § 1969. Sale Subject to Some Liens, Free from Others.
- § 1970. Order Should Provide for Transfer of Rights to Proceeds.
- § 1971. No Sale Free and Clear unless Reasonable Prospect of Surplus Appear or Lienholder Requests.
- § 1972. Parties Relegated to State Court Where Foreclosure Necessary to Bar Rights Not within Jurisdiction of Bankruptcy Court.
- § 1973. Also, Where Inchoate Dower Outstanding.
- § 1974. But, if Wife Consents, Sale May Be Made Free from Dower.
- § 1974½. Otherwise Where Dower Not Good against Levying Creditor.
- § 1975. Referee May Order Sale Free from Liens.
- § 1976. Even Free from Lien of Taxes.
- § 1977. Even before Validity and Priority of Liens Determined.
- § 1978. Even Where Located Outside of State, Provided Property Be Personality and in Actual Custody.
- § 1979. And Consent of Parties Not Necessary.
- § 1980. Notice to Lienholders Requisite.
- § 1981. No Established Form for Notice.
- § 1982. "Order to Show Cause," Approved Form of Notice.
- § 1983. Record of Referee to Show Notice and to Whom Given.
- § 1984. Procedure in Referee's Court to Follow Equity Rules Where Bankruptcy Rules Silent.
- § 1985. How Lienholder to Set Up Lien.
- § 1985½. Statutory Regulations of Party's Right to Maintain Suit, Not Binding.
- § 1986. Separate Accounts of Each Fund to Be Kept.
- § 1987. Failure to Object to Sale without Separation Waives Rights.
- § 1988. Taking Additional Evidence, after Sale, to Fix Proportions of Fund.
- § 1989. Expenses of Preservation and Sale Paid Out of Particular Fund Involved.
- § 1990. Each Fund to Bear Its Own Expenses and Costs.
- § 1991. Proportionate Part Not to Be Charged against Each Lien.
- § 1992. Costs and Expenses First Deducted and Liens Paid Out of Remainder.
- § 1993. General Costs of Administration Not Chargeable.
- § 1994. Trustee's Attorney's Fees and Expenses Benefiting Entire Fund Chargeable but Not Services for Litigating Liens.
- § 1995. Referee Has Authority to Tax Costs and Expenses.
- § 1996. Costs and Expenses Taxable.
- § 1997. Lienholder as Purchaser, May Apply Lien on Price, Except as to Superior Liens.

§ 1997½. Interest.

§ 1998. Trustee's Deed or Bill of Sale.

§ 1999. Remedies against Purchaser.

§ 2000. Jurisdiction of Suit by Third Party against Purchaser from Trustee.

§ 2000½. Whether Injunction Available in Aid of Purchaser to Protect against Third Party.

§ 2000¾. Trustee of Mortgage Bondholders, Whether to Be Paid by Trustee in Bankruptcy.

§ 1963. May Be Sold Subject to Liens.—The property may be sold subject to liens.¹ Even subject to the liens of taxes.²

§ 1964. If Not Mentioned to Be Otherwise, Sale Is Subject to Liens.—If the sale is not expressly ordered to be free and clear of liens, it will be a sale subject to liens.³

The sale of property "free from liens" must be taken to mean a sale free from such liens as were mentioned in the petition for sale.

In *re Crowell*, 29 A. B. R. 308, 199 Fed. 659 (D. C. Mass.): "The petitioner rests its claim upon the contention that its purchase of the lot under the order of sale has entitled it to have the land free of any lien or incumbrance at the time it paid the balance of the agreed purchase money and took the trustee's deed. The referee's order to sell, made on February 28, 1911, neither had nor could have had any application to the lien afterward created by the assessment of these taxes. Not only had no such lien then come into being, but what the lien or incumbrances were to which the referee's order referred appears from the petition for the order. This set forth that there were certain mortgages on the land; that one of the mortgages was to the petitioner for review and its validity disputed; that the land had been conveyed subject to conditions; and that it had been attached. To the validity, as against him, of any order to sell free from incumbrances, it is essential that a lienholder whose rights may be affected should have had due opportunity to defend his interest, and due notice to appear for that purpose. *Ray v. Norseworthy*, 22 Wall. 128, 135, 23 L. Ed. 116; In *re Platteville Foundry & Machine Co.* (D. C., Wis.), 17 Am. B. R. 291, 147 Fed. 828. The lienholders named as above in the petition for sale are the only lienholders who could have had such notice, or who could have been affected by the order. No other lienholders can be supposed to have been within the contemplation of the court in making the order for sale, or of the trustee in advertising the sale, or of the purchaser or other bidders at the sale. Since no lien for these taxes existed when the order was made, or the sale advertised, or when the sale thus ordered and advertised took place, no such lien was or could have been removed from the property or transferred to the proceeds by virtue of the order and the sale made in pursuance thereof. What the trustee received from the purchaser at the sale, and now holds, he must be considered to hold as representing the property freed from those liens which the petition described, if any, but freed from no others."

1. In *re Gerry*, 7 A. B. R. 459, 112 Fed. 958 (D. C. Pa.). Sup. Court's Official Form, No. 44. Compare, In *re Crowell*, 29 A. B. R. 309, 199 Fed. 659 (D. C. Mass.).

2. In *re Gerry*, 7 A. B. R. 459, 112 Fed. 958 (D. C. Pa.). Compare, where taxes became lien after order of sales

issued, In *re Crowell*, 29 A. B. R. 309, 199 Fed. 659 (D. C. Mass.).

3. In *re Foundry & Machine Co.*, 17 A. B. R. 293 (D. C. Wis.); In *re Crowell*, 29 A. B. R. 309, 199 Fed. 659 (D. C. Mass.); *obiter*, *McKay v. Hamill*, 26 A. B. R. 164, 185 Fed. 11 (C. C. A. Pa.).

§ 1965. May Be Sold Free from Liens and Liens Transferred to Proceeds.—The property may be sold free from liens and encumbrances, and the liens be transferred to the proceeds.

No form was prescribed for this purpose by the Supreme Court, and no special authorization of sales free from liens is to be found in the statute itself; but, so far as statutory authorization is concerned, nothing is found in the statute specially authorizing sales subject to liens, nor at private sale nor of perishable property, and yet those methods of sale are deemed proper in bankruptcy. And it would be a serious defect were it not permissible to sell property in bankruptcy free from liens, because such is ordinarily the best method of selling property. To sell property free and clear from all liens and to have all controversies relative to the validity and extent of liens thereon transferred to the fund, is likely to lead to better prices. Otherwise, the purchaser would have to buy all the controversies along with the purchase of the property itself. And the right to sell property in the bankruptcy court clear and free from all encumbrances, and to transfer the liens to the proceeds, is now beyond dispute.⁴

In re New England Piano Co., 9 A. B. R. 767, 122 Fed. 937 (C. C. A. Mass.): "The first proposition of the petition is that the District Court had no authority or jurisdiction to order a sale of the property in question free and clear of in-

4. See similar subject "Marshaling of Liens, etc.," ante, § 1963, et seq. [1841] In re Christy, 3 How. (U. S.) 292; obiter, In re Foundry & Machine Co., 17 A. B. R. 293 (D. C. Wis.); In re Worland, 1 A. B. R. 450, 92 Fed. 893 (D. C. Ia.); In re Sanborn, 3 A. B. R. 54, 96 Fed. 551 (D. C. Vt.); [1841] *Houston v. Bank*, 6 How. 486; [1867] *Ray v. Norseworthy*, 23 Wall. 128; In re Granite City Bk., 14 A. B. R. 404, 137 Fed. 818 (D. C. Md.); instance, In re Kellogg, 10 A. B. R. 11, 121 Fed. 333 (C. C. A. N. Y., affirming 7 A. B. R. 632); inferentially, obiter, In re Gerdes, 4 A. B. R. 346, 102 Fed. 318 (D. C. Ohio); Southern Loan & Trust Co. v. Benbow, 3 A. B. R. 10, 96 Fed. 514 (D. C. N. Car., reversed, on other grounds, in 3 A. B. R. 710); In re Waterloo Organ Co., 9 A. B. R. 427, 118 Fed. 904 (D. C. N. Y.); impliedly, In re Shoe & Leather Reporter, 12 A. B. R. 248, 129 Fed. 588 (C. C. A. Mass.); compare, query, obiter, *Chauncey v. Dyke Bros.*, 9 A. B. R. 444, 119 Fed. 1 (C. C. A. Ark., affirming In re Matthews, 6 A. B. R. 96).

Instances, In re Kellogg, 7 A. B. R. 632, 113 Fed. 113 (D. C. N. Y., affirmed in 10 A. B. R. 7, 121 Fed. 333); *McNair v. McIntyre*, 7 A. B. R. 638, 113 Fed. 120 (C. C. A. N. C.); In re Keller, 6 A. B. R. 351, 109 Fed. 131 (D. C. Iowa); Taxes on merchandise sold by trustee

in bulk free and clear where State Statute makes such taxes a lien. In re Utt, 5 A. B. R. 383, 105 Fed. 754 (C. C. A. Ills.).

In re Waterloo Organ Co., 18 A. B. R. 752, 154 Fed. 657 (C. C. A. N. Y.); In re Littlefield, 19 A. B. R. 18, 155 Fed. 838 (C. C. A. N. Y.), quoted at § 1967; In re Miner's Brewing Co., 20 A. B. R. 717, 162 Fed. 327 (D. C. Pa.); In re Dana, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.), quoted at § 1885; obiter, In re Allert, 23 A. B. R. 101, 173 Fed. 691 (D. C. N. Y.); instance, sale by receiver, In re Vogt, 20 A. B. R. 457, 159 Fed. 317, 163 Fed. 551 (D. C. N. Y.); In re Kronrot, 25 A. B. R. 738, 183 Fed. 653 (D. C. N. Y.); In re Torchia, 26 A. B. R. 188, 185 Fed. 576 (D. C. Pa.); In re [Wolf] Freedman, 31 A. B. R. 53, — Fed. — (D. C. N. Y.); obiter, In re Vulcan F'd & Mach. Co., 24 A. B. R. 825, 180 Fed. 671 (C. C. A. Pa.), quoted at § 1993; obiter, In re Davis, 25 A. B. R. 1, 180 Fed. 148 (D. C. N. Y.); Instances, In re Crowell, 29 A. B. R. 309, 199 Fed. 659 (D. C. Mass.); instance, In re Britannia Min. Co., 28 A. B. R. 651, 197 Fed. 459 (D. C. Wis.); In re Arden, 26 A. B. R. 684, 188 Fed. 475 (D. C. N. Y.); In re Zehner, 27 A. B. R. 537, 193 Fed. 787 (D. C. La.); In re Kinsey Co., 25 A. B. R. 651, 184 Fed. 694 (C. C. A. Ohio).

cumbrances. The petitioner concedes the force of the decisions of the Supreme Court in *In re Christy*, 3 How. 292, and *Ray v. Norseworthy*, 23 Wall. 128, already referred to; but it claims that the former was under the Bankruptcy Act of 1841, and the latter under that of 1867, and that both of those statutes expressly conferred powers on the District Court sitting in bankruptcy which are not given it by the act of 1898. Even if this were so, it would not follow that a decree should be entered in favor of the petitioner. By § 2 of the act of 1898 the District Courts as courts of bankruptcy are given 'such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in bankruptcy proceedings in vacation in chambers, and during their respective terms.' As we have shown in other opinions, the District Court sitting in bankruptcy proceeds in accordance with the principles of equity, and exercises equitable powers. An order like this appealed from is clearly within the ordinary jurisdiction of courts proceeding on those principles and exercising those powers. *In re Christy* fully recognizes this principle at pages 312 and 313. The case was reaffirmed in *Nugent v. Boyd*, 3 How. 426, and *Houston v. City Bank*, 6 How. 486. In this connection the petitioner claims that *Ray v. Norseworthy* was rested on § 20 of the act of 1867, which gave special powers with reference to creditors wholly or partially secured, offering proofs of debts against bankrupt estates; but an examination of the opinion shows that the case was merely supported by the reference to that section, and that the first section of the act was regarded as wholly sufficient. Nothing cited from the act of 1841 in *In re Christy* vested in the District courts sitting in bankruptcy any greater powers than are found in the provisions of § 2 of the present statute, giving them jurisdiction 'at law and in equity,' as we have already said, and authorizing them to 'cause the estates of bankrupts to be collected, reduced to money, and distributed,' and to 'make such orders, issue such process, and enter such judgments, in addition to those specifically provided for, as may be necessary for the enforcement of the provisions' of the act."

Sturgis v. Corbin, 15 A. B. R. 545, 141 Fed. 1 (C. C. A. W. Va.): "The order of the court below directing a sale of the property clear of all liens, claims and incumbrances was, under the circumstances, a wise exercise of judicial discretion, being such action as the Bankrupt Act contemplates and provides for in those instances where the nature and location of the property make it desirable in the interest of creditors that the same be sold as soon as practicable."

In re Roger Brown & Co., 28 A. B. R. 336, 196 Fed. 758 (C. C. A. Iowa): "The present bankruptcy law makes no express provision for sale by the trustee free of incumbrance, but it is uniformly held that he may be authorized to so sell if there are reasonable grounds for believing that more could be realized than the amount of the encumbrance."

In re Kest, 11 A. B. R. 117, 128 Fed. 651 (D. C. Pa.): "There can be no question as to the authority of the District Court * * * . This is essential to a complete administration of the bankrupt's estate, and will be implied from the general provisions of the present act, even though not expressly given, as in the preceding Act of 1867."

In re Pittelkow, 1 A. B. R. 472, 92 Fed. 901 (D. C. Wis.): "Upon the general question of jurisdiction, I am of the opinion that the District Court is vested with exclusive jurisdiction over the property of the bankrupt, and with sufficient equity powers to have all claims by mortgagees brought in and administered; that sales may be authorized, under proper circumstances, free and clear from the mortgages, or other liens, by preserving and transferring the claims to the fund thus provided; and that the commencement of foreclosure proceedings can be restrained to that end."

In *re Prince & Walter*, 12 A. B. R. 678, 131 Fed. 546 (D. C. Pa.): "But, notwithstanding what has been said above about liens unaffected by bankruptcy proceedings, it is in the power of the court to order a sale clear and free of them, regardless of how they would ordinarily stand."

And it may be sold free, even, from the lien of taxes;⁵ though not to the prejudice of the state or municipality.

And the power of the bankruptcy court to sell free and clear from liens is discretionary and not subject to collateral attack.⁶

The provisions of the Bankruptcy Act that valid liens shall not be affected by bankruptcy proceedings has reference only to the validity of the contract, and not to the remedy nor forum for enforcing the lienholder's rights, which may be changed without impairing the contractual obligation, providing an equally adequate and efficient remedy is substituted.⁷

§ 1966. Lienholder's Consent Not Necessary.—And it does not require the lienholder's consent.⁸

It is clear that, by agreement, property also may be sold clear and free and the liens transferred to the fund;⁹ and the agreement may be implied.¹⁰

§ 1967. Sale Clear and Free Ordered before Validity or Priority of Liens Determined.—A sale free and clear from liens may be ordered before the validity and priority of the liens have been determined, the controversies being transferred to the funds.¹¹

In *re Littlefield*, 19 A. B. R. 18, 155 Fed. 838 (C. C. A. N. Y.): "A court of bankruptcy has jurisdiction to order a sale of a bankrupt's property upon which a lien is asserted without first determining either the validity or amount of the lien."

In *re Shoe & Leather Reporter*, 12 A. B. R. 248, 129 Fed. 588 (C. C. A.): "After a full investigation, the District Court, sitting in bankruptcy, ordered

5. In *re Prince & Walter*, 12 A. B. R. 678, 131 Fed. 546 (D. C. Pa.); In *re Keller*, 6 A. B. R. 351, 109 Fed. 131 (D. C. Iowa).

6. *Equitable Trust Co. v. Vanderbilt Realty Co.*, 31 A. B. R. 834 (N. Y. Sup. Ct. App. Div.).

7. In *re Zehner*, 27 A. B. R. 536, 193 Fed. 787 (D. C. La.).

8. *Geo. Carroll & Bro. Co. v. Young*, 9 A. B. R. 643, 119 Fed. 577 (C. C. A. Pa.). See most of the cases cited in the preceding paragraph, § 1965. In *re Dana*, 21 A. B. R. 683, 167 Fed. 529 (C. C. A.), quoted at § 1885; *obiter*, In *re Allert*, 23 A. B. R. 101, 173 Fed. 691 (D. C. N. Y.); In *re Kinsey Co.*, 25 A. B. R. 651, 184 Fed. 694 (C. C. A. Ohio); In *re Howard*, 31 A. B. R. 251, 207 Fed. 402 (D. C. N. Y.); *obiter*, In *re Chambersburg Mfg. Co.*, 26 A. B. R. 107, 190 Fed. 411 (D. C. Pa.), quoted at § 1971. *Contra*, In *re Fite*, 31 A. B. R. 308 (Ref. Pa.).

9. In *re Bourlier Cornice & Roofing Co.*, 13 A. B. R. 585 (D. C. Ky.); In *re Kronrot*, 25 A. B. R. 738, 183 Fed. 653 (D. C. N. Y.); *obiter*, In *re Zehner*, 27 A. B. R. 536, 193 Fed. 787 (D. C. La.).

10. *Chauncey v. Dyke Bros.*, 9 A. B. R. 444, 119 Fed. 1 (C. C. A. Ark.); In *re Chambersburg Mfg. Co.*, 26 A. B. R. 107, 190 Fed. 411 (D. C. Pa.).

11. In *re Granite City Bank*, 14 A. B. R. 405, 408, 137 Fed. 818 (C. C. A. Iowa, affirming In *re Wilka*, 12 A. B. R. 727); In *re Union Trust Co.*, 9 A. B. R. 767, 112 Fed. 937 (C. C. A. Mass.); *instance*, In *re Waterloo Organ Co.*, 9 A. B. R. 427, 118 Fed. 904 (D. C. N. Y.); *Mason v. Wolkowich*, 17 A. B. R. 709, 150 Fed. 699 (C. C. A. N. Y.); In *re Tucker* (*Tucker v. Curtin*), 18 A. B. R. 378, 153 Fed. 91 (C. C. A. N. Y.), although in this case the decision does not show on its face that the point was decided—only by reference to *Mason v. Wolkowich*.

a sale of all the assets, leaving all questions as to what portions thereof are covered by the mortgage and are not covered by it to be afterwards ascertained and determined. Therefore, so far as the main issue is concerned, the District Court rested securely on our decision in *Union Trust Company, Petitioner*."

§ 1968. But Not Where Lienholder Who Desires to Bid, Objects.—But a sale free and clear, before the priority, validity and extent of liens have been determined, should not be ordered over the objection of a lienholder who might desire to bid and use the ascertained value of his lien in part payment of the purchase price.¹²

§ 1969. Sale Subject to Some Liens, Free from Others.—The sale may be ordered subject to some liens and free from others;¹³ and failure to mention a lien makes the sale subject thereto.¹⁴

§ 1970. Order Should Provide for Transfer of Rights to Proceeds.—In selling free from liens the order of sale should provide for the transfer of the liens to the proceeds.¹⁵

In *re Kohl-Hepp Brick Co.*, 23 A. B. R. 822, 176 Fed. 340 (C. C. A. N. Y.): "This order was made after appellants had given notice of their alleged lien, but it makes no provision for the imposition of such lien on the proceeds of sale. Under the authorities such provisions are essential."

§ 1971. No Sale Free and Clear unless Reasonable Prospect of Surplus Appear or Lienholder Requests.—The bankruptcy court generally will not order a sale free from liens unless there is a reasonable prospect that a surplus will be left for general creditors, or some lienholder requests it: that the interests of the general creditors will be advanced and the interests of lienholders not injuriously affected.¹⁶

12. In *re Saxton Furnace Co.*, 14 A. B. R. 483 (D. C. Pa.); In *re Fayetteville, etc., Co.*, 28 A. B. R. 307, 197 Fed. 180 (D. C. Ark.).

13. Instance, ordered sold subject to first mortgage, free as to second mortgage, taxes (circumstances as to taxes peculiar, however) and other liens, In *re Prince & Walter*, 12 A. B. R. 675, 131 Fed. 546 (D. C. Pa.).

14. In *re Foundry & Machine Co.*, 17 A. B. R. 293 (D. C. Wis.); In *re Crowell*, 29 A. B. R. 309, 199 Fed. 659 (D. C. Mass.). Compare, *McKay v. Hamill*, 26 A. B. R. 164, 185 Fed. 11 (C. C. A. Pa.), where all parties concerned in the sale considered it as being made free from all liens.

15. In *re Goldsmith*, 9 A. B. R. 419, 118 Fed. 763 (D. C. Tex.), quoted at § 1971; *obiter*, In *re Vulcan F'd & Mach. Co.*, 24 A. B. R. 825, 180 Fed. 671 (C. C. A. Pa.), quoted at § 1993.

Selling Free from Landlord's Lien, Landlord Required to Look to Pur-

chaser Instead of Proceeds, When.—

In one case the court relegated the landlord to his rights against the purchaser of the leasehold rather than paying him his lien out of the proceeds of the sale of the property on the premises. In *re Varley & Bauman Co.*, 26 A. B. R. 104, 188 Fed. 761 (D. C. Ala.).

16. In *re Cogley*, 5 A. B. R. 731, 107 Fed. 73 (D. C. Iowa); *obiter*, In *re Keet*, 11 A. B. R. 117, 128 Fed. 651 (D. C. Pa.); In *re Gibbs*, 6 A. B. R. 485, 109 Fed. 627 (D. C. Vt.); In *re Barber*, 3 A. B. R. 306, 97 Fed. 547 (D. C. Minn.); In *re Shaeffer*, 5 A. B. R. 248, 105 Fed. 352 (D. C. Pa.); [1867] In *re Dillard*, 2 Hughes 190, Fed. Cases, No. 3,912; instance, In *re Alden*, 16 A. B. R. 380 (Ref. Ohio.); In *re Fayetteville Wagon-Wood & Lumber Co.*, 28 A. B. R. 307, 197 Fed. 180 (D. C. Ark.); In *re Rose*, 26 A. B. R. 752, 193 Fed. 815 (D. C. Ky.); In *re Roger Brown & Co.*, 28 A. B. R. 336, 196 Fed. 758 (C. C. A. Iowa); In *re Holmes Lumber Co.*, 26

Obiter, *In re Roger Brown Co.*, 28 A. B. R. 336, 196 Fed. 758 (C. C. A. Iowa): "If such property is so encumbered that nothing can be realized above the encumbrance it is the duty of the trustee to abandon the property, but in this case the property was appraised at fifteen thousand dollars and the trustee and referee both had reason to think something would be realized above the mortgage."

Obiter, *In re New England Piano Co.*, 9 A. B. R. 770, 122 Fed. 937 (C. C. A. Mass.): "It is true that, ordinarily, the court in bankruptcy ought not to interfere in this way where it is apparent that the estate has no equity of redemption of value, but this cannot be held to be universally true for reason which we have no occasion to state."

In re Chambersburg Mfg. Co., 26 A. B. R. 107, 190 Fed. 411 (D. C. Pa.): "The exceptants reply that they should not be obliged to contribute of their security since they have steadfastly protested to its discharge by sale. While the bankruptcy court had the authority to discharge the lien without their consent, and order certain costs incident to the same paid out of the fund, notwithstanding, this is a power which is exercised with great care and caution, and any defalcation for costs and fees is jealously guarded."

In re Pittelkow, 1 A. B. R. 472, 92 Fed. 901 (D. C. Wis.): "It is, however, the duty of the court to consider the interests of mortgagees and other secured creditors as well as those of the general creditors; and unless it is apparent (1) that the mortgaged premises in the given case will probably realize upon a sale an amount substantially in excess of the mortgage, and (2) that there are no complications, by dower rights, conveyances, or other conditions, which require foreclosure under the mortgage, the power to proceed summarily by sale, including the interest of the mortgagee, should not be exercised."

In re Styer, 3 A. B. R. 424, 98 Fed. 290 (D. C. Pa.): "Assuming * * * that such power exists, it is clear that the sale should not be ordered unless the court is satisfied that the interest of general creditors would be thus advanced, and that the interest of the lien creditors would not be injuriously affected."

In re Goldsmith, 9 A. B. R. 426, 118 Fed. 763 (D. C. Tex.): "In the administration of bankruptcy estates it has been the rule to carefully consider whether there is a probable interest in incumbered property for the general creditors; if it be decided there is, then to sell same, after notice, either subject to or free from incumbrance, as conditions may indicate. If sold free from incumbrance, it ought to be provided that such incumbrances, and liens as may be found to exist should attach to the proceeds of the sale. If it be decided there is no interest for the general creditors, then the bankruptcy court should not undertake to administer the property for an absent lienor. To undertake its administration is an abuse of discretion justly condemned by the authorities."

But where the validity of liens, or the extent of liens upon after-acquired property, is in dispute, in such way that the question of a possible surplus is in doubt, sale, free and clear, will be ordered.¹⁷

A. B. R. 119, 189 Fed. 178 (D. C. Ala.); *In re Arden*, 26 A. B. R. 684, 188 Fed. 475 (D. C. N. Y.). Compare, *Equitable Trust Co. v. Vanderbilt Realty Co.*, 31 A. B. R. 834 (N. Y. Sup. Ct. App. Div.); inferentially merely, *In re Vulcan F'dy & Mach. Co.*, 24 A. B. R. 825, 180 Fed.

671 (C. C. A. Pa.) quoted at § 1993; compare, where trustee disputed validity of mortgage, *In re Zehner*, 27 A. B. R. 536, 193 Fed. 787 (D. C. La.).

¹⁷ *In re New England Piano Co.*, 9 A. B. R. 772, 122 Fed. 937 (C. C. A. Mass.).

And the court may, in its discretion, order a sale free and clear of liens, although the encumbrances thereon equal the value of the property.¹⁸

In *re Keet*, 11 A. B. R. 117, 128 Fed. 651 (D. C. Pa.): "It is not therefore a matter of power, but of discretion, and while, ordinarily, the latter will not be exercised in favor of a sale where the encumbrances equal the value of the property * * * yet there are considerations in the present instance which seem to make it desirable."

A sale clear and free of liens will be ordered, if a reasonable prospect of surplus for general creditors appears, other things being equal.

In *re Zehner*, 27 A. B. R. 537, 193 Fed. 787 (D. C. La.): "However, the application is for leave to foreclose in the state court and the trustee has not seen fit to abandon the mortgaged property. On the contrary, he strenuously asserts there is a considerable equity in it that will benefit the general fund, and he does not admit the validity of the petitioner's mortgage. * * * The jurisdiction of the state court to sell the property of the bankrupt even after adjudication is concurrent with that of the federal court, and the latter jurisdiction is only exclusive by reason of its custody of the res. * * * But it seems to me, however, that in all cases where it is probable that a surplus will be realized over and above the liens and mortgages, or even in doubtful cases, it would be better for all parties concerned that the property be sold through the bankruptcy court."

But the costs of such sale must be taken from the fund realized from the encumbered property, and must not be taken from general creditors.¹⁹

The time to object to a sale free and clear is before the sale, and parties are not entitled to wait until afterwards.

It was held in one case, to be sure, that the Amendment of 1910 to Bankruptcy Act, § 48, providing for commissions on amounts paid to lienholders, as well as to others, is not applicable to cases where the property brings "largely less" than the concededly valid encumbrances, the court arguing that such deficiency is itself *prima facie* proof that the bankruptcy court had not "rightfully exercised its jurisdiction to sell free from liens;" but it would seem that the objection to such sale should have been by the lienholder at the start, when first summoned into court, according to the ordinary rules, or at any rate before the sale had been made; and that his failure so to object was itself, rather, *prima facie* proof, and at least an admission by the lienholder, that the sufficiency or insufficiency of the price likely to be obtained was so entirely unknown and unascertainable that it would be a proper exercise of the bankruptcy court's jurisdiction to order a sale.

In *re Foster*, 25 A. B. R. 96, 181 Fed. 703 (D. C. Vt.): "Property of a bankrupt, incumbered by mortgage liens given in good faith and duly recorded more

18. In *re Cogley*, 5 A. B. R. 731, 107 Fed. 73 (D. C. Iowa).

And it has been held that the judicial discretion so exercised is not subject to

review. In *re Throckmorton*, 28 A. B. R. 487, 196 Fed. 656 (C. C. A. Ohio).

19. In *re Cogley*, 5 A. B. R. 731, 107 Fed. 73 (D. C. Iowa).

than four months before the filing of the petition in bankruptcy, should be carefully inquired into before an order of sale is made, and it should appear that such liens will not be affected by the sale and the bankrupt estate will be benefited thereby provided, as in this case, the mortgagee makes no claim against the bankrupt estate."

§ 1972. Parties Relegated to State Court Where Foreclosure Necessary to Bar Rights Not within Jurisdiction of Bankruptcy Court.—But where foreclosure is necessary to bar rights which cannot be brought before the bankruptcy court, the bankruptcy court will relegate the parties to the state courts.²⁰

Obiter, *In re Pittelkow*, 1 A. B. R. 472, 92 Fed. 901 (D. C. Wis.): "Certainly, if foreclosure is necessary to bar rights which cannot be brought before the court of bankruptcy proceedings, the mortgagee should have leave to that end, on proper showing of cause; otherwise, he would be compelled to bid for the protection of his mortgage interest, without the benefits of complete foreclosure."

Or, at any rate, will permit the parties to resort to the State courts to effect the foreclosure.

In re Victor Color & Varnish Co., 23 A. B. R. 177, 175 Fed. 1023 (C. C. A. N. Y.): "We are clearly of the opinion that the holder of the chattel mortgage was entitled to have his day in court, in a suit to foreclose it, and that so much of the order as refused him leave to begin such a suit, on the ground that the property was in the hands of a receiver in bankruptcy, must be reversed. It was entirely proper, however, for the bankruptcy court to refuse to give petitioner immediate possession of the property; it should remain in the custody of the receiver till the suit is determined, although, of course, if all parties agree, it may be sold and the proceeds held by the receiver. Order modified."

The bankruptcy court has power to sell free from liens, but not to "foreclose."²¹

Thus, it is possible for the bankruptcy court to sell assets free from liens, transferring the liens to the proceeds of sale, and at the same time allow the lienholder to maintain a suit to foreclose his lien in the State court.²²

• **§ 1973. Also, Where Inchoate Dower Outstanding.**—Also, where the wife's inchoate dower is outstanding, the parties may be relegated to the state court where inchoate dower can be cut off.²³

^{20.} *In re Shaeffer*, 5 A. B. R. 248, 104 Fed. 973 (D. C. Pa.). *In re Fayetteville Wagon-Wood & Lumber Co.*, 28 A. B. R. 307, 197 Fed. 180 (D. C. Ark.). Compare, analogously, ante, §§ 1584, 1584½, 1806; but also compare, § 1813.

^{21.} Compare, inferentially, *Good-nough Mercantile & Stock Co. v. Gallo-way*, 19 A. B. R. 244, 156 Fed. 504 (D.

C. Ore.). Compare, though merely inferentially, *In re Chambersburg Mfg. Co.*, 26 A. B. R. 107, 190 Fed. 411 (D. C. Pa.).

^{22.} Instance, on the facts, *In re Clover Creamery Ass'n*, 23 A. B. R. 884, 176 Fed. 907 (C. C. A. Wis.).

^{23.} *In re Shaeffer*, 5 A. B. R. 248, 104 Fed. 973 (D. C. Pa.).

§ 1974. But, if Wife Consents, Sale May Be Made Free from Dower.—But, if the wife consents, a sale may be ordered in the bankruptcy court free from her inchoate dower rights, and she may be compensated therefor out of the proceeds.²⁴ And this practice is approved.

Savage v. Savage, 15 A. B. R. 599, 141 Fed. 346 (C. C. A. Va.): "With regard to the objection urged against the order to sell bankrupt's remaining real estate free from the wife's contingent right of dower, it is sufficient to say that it is nearly always desirable, in making sale of a bankrupt's real estate, if the wife will consent, to sell free from her inchoate right of dower, and to compensate her by a fair allowance out of the proceeds for her release of that right. It is common practice to do so when it is possible, and we think the practice is to be approved, as it gives the purchaser an unincumbered title, and ordinarily results in advantage to creditors by obtaining a better price for a clear title than can be obtained for property the title to which is clouded by such a possible incumbrance."

And where she does consent, then the value of her dower right is to be computed in accordance with state law.²⁵ Where the wife gives consent to such sale, she may, on sale being made, be compelled to execute a formal release of the dower.²⁶

§ 1974½. Otherwise Where Dower Not Good against Levying Creditor.—But where, as in Pennsylvania, dower is not good against a levying creditor, it will not be available against the trustee, since the Amendment of 1910 to § 47 (a) (2) gives the trustee the rights and remedies of a creditor armed with process; and in such states the property may be sold free and clear of dower.²⁷

§ 1975. Referee May Order Sale Free from Liens.—The referee may order the sale free from liens and the transfer of the liens to the proceeds of the sale.²⁸

24. In re Acretelli, 21 A. B. R. 537, 173 Fed. 121 (D. C. N. Y.). Instance, In re Lingafelter, 24 A. B. R. 656, 181 Fed. 24 (D. C. A. Ohio); instance, In re Hays, 24 A. B. R. 669, 181 Fed. 674 (C. C. A. Ohio).

25. In re Forbes, 7 A. B. R. 42 (Ref. Ohio), computed on equity of redemption in Ohio, whenever purchase money mortgage exists. In re Hawkins, 9 A. B. R. 598 (D. C. R. I.), computed on entire value of the land payable out of the equity of redemption.

26. In re Acretelli, 21 A. B. R. 537, 173 Fed. 121 (D. C. N. Y.): "The right to make the sale presupposes the power to compel it (the consent once given)."

27. In re Codori, 30 A. B. R. 453, 207 Fed. 784 (D. C. Pa.), quoted at § 1166¼; Instance, In re Freedman, 29 A. B. R. 135 (Ref. Pa. affirmed 31 A. B. R. 53, — Fed. — D. C.).

28. *Obiter*, In re Foundry & Machine Co., 17 A. B. R. 293 (D. C. Wis.); *obiter*, *Chauncey v. Dyke Bros.*, 9 A. B. R. 444, 119 Fed. 1 (C. C. A. Ark., affirming In re Matthews, 6 A. B. R. 96); In re Sanborn, 3 A. B. R. 54, 96 Fed. 551 (D. C. Vt.); In re Styer, 3 A. B. R. 424, 98 Fed. 290 (D. C. Pa.); In re Matthews, 6 A. B. R. 96, 109 Fed. 603 (affirmed sub. nom. *Chauncey v. Dyke Bros.*, 9 A. B. R. 444, 119 Fed. 1, C. C. A. Ark.); In re Kellogg, 7 A. B. R. 623, 113 Fed. 120-122 (D. C. N. Y.); In re Pittelkow, 1 A. B. R. 472, 92 Fed. 901 (D. C. Wis.); In re Granite City Bank, 14 A. B. R. 404, 137 Fed. 818 (C. C. A. Iowa, affirming In re Wilka, 12 A. B. R. 727); inferentially, In re Saxon Furnace Co., 14 A. B. R. 483, 136 Fed. 697 (D. C. Pa.).

Instances, In re Goldsmith, 9 A. B. R. 419, 118 Fed. 763 (D. C. Tex.); In re Prince & Walter, 12 A. B. R. 675, 131 Fed. 546 (D. C. Pa.); In re New Eng-

In re Waterloo Organ Co., 9 A. B. R. 427 (D. C. N. Y.): "It is in the province of the referee to direct the manner of sale free and clear from incumbrances, and he may preserve and transfer bona fide liens to the fund, arising from the same."

§ 1976. Even Free from Lien of Taxes.—Even free from the lien of taxes.²⁹

§ 1977. Even before Validity and Priority of Liens Determined.—Even before the validity of liens and their priority have been determined.³⁰ But not where there is objection and one of the lienholders may desire to bid on the property and use the value of his lien in part payment of the purchase price.³¹

§ 1978. Even Where Located Outside of State, Provided Property Be Personalty and in Actual Custody.—Even where located outside the state, at any rate where the property is personalty, and is reduced to the actual custody of the trustee.³²

§ 1979. And Consent of Parties Not Necessary.—And consent of parties is not necessary before the referee may act.³³

The property may be sold, by consent, free from exemptions, and the exemptions paid out of the proceeds.³⁴ But such sale of exempt property by consent of parties will not dispense with the requirements of § 7 (a) that the bankrupt shall make formal claim in Schedule B (5) therefor.

§ 1980. Notice to Lienholders Requisite.—Notice must be given to the lienholders.³⁵

In re Noel, 14 A. B. R. 720, 137 Fed. 694 (D. C. Md.): "That court having

land Piano Co., 9 A. B. R. 767, 122 Fed. 937 (C. C. A. Mass.); Carriage Co. v. Solanas, 6 A. B. R. 225, 108 Fed. 532 (D. C. La.); In re Rosenberg, 8 A. B. R. 624, 116 Fed. 402 (D. C. Pa.); In re Keller, 6 A. B. R. 351, 109 Fed. 131 (D. C. Iowa); McNair v. McIntyre, 7 A. B. R. 638, 113 Fed. 113 (C. C. A. N. Car.); In re Miner's Brewing Co., 20 A. B. R. 717, 162 Fed. 327 (D. C. Pa.). See ante, § 1888.

^{29.} In re Prince & Walter, 12 A. B. R. 675, 131 Fed. 546 (D. C. Pa.); In re Keller, 6 A. B. R. 351, 109 Fed. 131 (D. C. Iowa).

^{30.} Impliedly, In re Granite City Bk., 14 A. B. R. 405, 137 Fed. 818 (C. C. A. Iowa). In re Manistee Watch Co., 28 A. B. R. 316, 197 Fed. 455 (D. C. Mich.).

^{31.} In re Saxton Furnace Co., 14 A. B. R. 483, 136 Fed. 697 (D. C. Pa.).

^{32.} In re Wilka, 12 A. B. R. 727, 131 Fed. 904 (D. C. Iowa, affirmed sub nom. In re Granite City Bk., 14 A. B. R. 404, 137 Fed. 818).

^{33.} Impliedly, In re Granite City Bank, 14 A. B. R. 404, 137 Fed. 818 (C. C. A. Iowa, affirming In re Wilka, 12 A. B. R. 727, 131 Fed. 904). Compare, to same effect, ante, § 1886.

^{34.} See cases cited under this head in the chapter treating of exemptions, ante, § 1089. Also, see In re Prince & Walter, 12 A. B. R. 675, 131 Fed. 546 (D. C. Pa.).

^{35.} See ante, § 1889: United Sheet & Tin Plate Co. v. Hess, 20 A. B. R. 254, 159 Fed. 889 (C. C. A. Ohio), quoted at § 1889; In re Kohl-Hepp Brick Co., 23 A. B. R. 822, 176 Fed. 340 (C. C. A. N. Y.), quoted also, at § 1970; obiter, In re Torchia, 26 A. B. R. 188, 185 Fed. 576 (D. C. Pa.), quoted at § 1990; In re Sanborn, 3 A. B. R. 54, 96 Fed. 551 (D. C. Vt.); In re Saxton Furnace Co., 14 A. B. R. 483, 136 Fed. 697 (D. C. Pa.); obiter, In re Gerdes, 4 A. B. R. 347, 102 Fed. 318 (D. C. Ala.). See cases cited ante, under "Marshaling of Liens," § 1963, et seq.

possession of the property, has jurisdiction, upon notice to those claiming to have liens and incumbrances upon it, to order the property to be sold by the trustees free of all incumbrances, if the court, in its discretion, should determine that such a sale was for the benefit of the unsecured creditors; and after such a sale, having in its control the fund arising from the sale, it would have jurisdiction to determine the conflicting claims of the parties whose lien had been displaced as to the property sold, and transferred to the fund in the court."

In *re Foundry & Machine Co.*, 17 A. B. R. 293, 147 Fed. 828 (D. C. Wis.): "Notice to the lien creditors of the application for sale must not only be given but the record must disclose affirmatively that every creditor whose lien will be discharged by the sale has received due notice of the application."

And a sale cannot divest the lien of a creditor unless he has been given such notice, and unless the sale has been made free therefrom.³⁶

In *re Kohl-Hepp Brick Co.*, 23 A. B. R. 822, 176 Fed. 340 (C. C. A. N. Y.): "This order was made after appellants had given notice of their alleged lien, but it makes no provision for the imposition of such lien on the proceeds of sale. Under the authorities such provisions are essential. * * * It is unfortunate to have to reverse the order at this late stage of the proceedings, but the power to displace liens is a drastic one, and should be exercised only with scrupulous attention to secure the lienor specific notice and full opportunity to protect his interests." Quoted further at § 1979.

Even though the claim of lien be considered "frivolous" the claimant should be given notice.³⁷

Although, without notice, the sale doubtless would not be invalid but would simply be a sale subject to whatever rights the claimant might succeed in establishing.

§ 1981. No Established Form for Notice.—There is no established form for such notice. It need not be in conformity with the summons or subpcena of plenary actions, unless required to be so by local rule of court.³⁸ Yet notice by mail undoubtedly would be insufficient, on default, to cut off rights.

36. See ante, § 1889. *Bassett v. Thacker*, 16 A. B. R. 787, 72 N. J. L. 81, 60 Atl. 39; In *re Foundry & Machine Co.*, 17 A. B. R. 293 (D. C. Wis.).

Consent of Lienholder's Attorney.—Instance, where held insufficient because record fails to show authority: In *re Foundry & Machine Co.*, 17 A. B. R. 294 (D. C. Wis.).

Equitable Trust Co. v. Vanderbilt Realty Co., 31 A. B. R. 834 (N. Y. Sup. Ct. App. Div.). Notice to trustees for bondholders and his appearance held sufficient.

No Notice on Lienholder, No Pleading of Lien Order Silent, Yet Purchase Protected and Lienholder Given Lien on Proceeds.—In one case where there

was at any rate irregularity and great informality, the court reversed the referee for holding that a lienholder was relegated to the purchaser where the purchaser had thought he was buying clear and free and had paid full value and the lienholder had been active in aiding the sale and had shared the purchaser's belief, the reviewing court giving the lienholder a lien on the proceeds. *McKay v. Hamill*, 26 A. B. R. 164, 185 Fed. 11 (C. C. A. Pa.).

37. In *re Kohl-Hepp Brick Co.*, 23 A. B. R. 822, 176 Fed. 340 (C. C. A. N. Y.).

38. Compare, evidently, In *re Granite City Bk.*, 14 A. B. R. 404 (C. C. A. Iowa).

§ 1982. "Order to Show Cause," Approved Form of Notice.—An "order to show cause" why a certain act should not be done, or a certain course pursued, is the regular and approved method of giving notice of contemplated action to parties to proceedings in bankruptcy, and would probably be the most appropriate form of notice in the marshaling of liens and sale of land.³⁹

§ 1983. Record of Referee to Show Notice and to Whom Given.—And the record of the referee should show not only that due notice was given, but what kind and length of notice were given.⁴⁰

And to whom the notice was given, mentioning specially the lienholders and others claiming to hold interests in the property.

In *re Saxton Furnace Co.*, 14 A. B. R. 483, 136 Fed. 697 (D. C. Pa.): "Moreover, the record should show affirmatively that every creditor whose lien will be discharged by the sale has received notice of the trustee's application to sell. The referee's general statement, that such notice 'was given to each and every general creditor and lien creditor,' is obviously insufficient. No doubt this is his opinion, and it may be true, but his record must show the facts by which other persons can verify the correctness of his statement."

§ 1984. Procedure in Referee's Court to Follow Equity Rules Where Bankruptcy Rules Silent.—In selling property free from liens, the method of procedure in the referee's court is to be gathered by analogy from the procedure in other sales in bankruptcy, aided by the equity rules prescribed by the United States Supreme Court in accordance with the Supreme Court's General Order No. XXXVII.⁴¹

§ 1985. How Lienholder to Set Up Lien.—It is not necessary for a secured creditor in such cases to make proof in the form prescribed by the Supreme Court for proof of secured claims: he may simply file an intervening petition setting up his lien, as in other cases.⁴² But he may, if he prefers, make proof in the form prescribed for proof of a secured claim in bankruptcy.⁴³

The right of amendment, of course, exists under the usual rules.

39. See post, §§ 2841, 2878, 2922. *Kuntz v. Young*, 12 A. B. R. 509, 131 Fed. 719 (C. C. A. Minn.); *In re Kinsey Co.*, 25 A. B. R. 651, 184 Fed. 694 (C. C. A. Ohio).

"Order to show cause" not appealable nor reviewable. *Morehouse v. Hardware Co.*, 24 A. B. R. 178, 177 Fed. 337 (C. C. A. Nev.).

40. Impliedly, Gen. Order XXIII. See ante, § 562.

41. Compare, *In re Pittelkow*, 1 A. B. R. 472 (D. C. Wis.).

42. *In re Goldsmith*, 9 A. B. R. 419, 118 Fed. 763 (D. C. Tex.); *Carriage Co. v. Solanas*, 6 A. B. R. 225 (D. C. La.); *In re Stevens*, 23 A. B. R. 239, 173 Fed. 342 (D. C. Ore.), quoted ante, at § 258½. To same effect, see ante, § 1894.

Apparently, contra, *In re Rosenberg*, 16 A. B. R. 465, 144 Fed. 442 (D. C. Pa.).

43. See ante, § 1894. *Burrows v. Grand Lodge*, 13 A. B. R. 545, 133 Fed. 708 (C. C. A. Tex.).

Secured Creditor Filing Proof of Claim Disclosing Security but Claim Allowed in Full without Deduction.—Where the secured creditor duly filed proof of debt in the prescribed form, setting up his security, and the claim was allowed in full without deduction of the value of the securities, it will be presumed the referee had found the securities to be of no value, but it will not work a forfeiture of the lien where the property is subsequently sold. *Bassett v. Thackara*, 16 A. B. R. 787, 72 N. J. L. 81, 60 Atl. 39.

In cases of amendment, the better practice undoubtedly is to present the proposed amendment at the time of the application for leave to amend.⁴⁴

Interest is computable to the date of payment of the lien, not to the date of the filing of the bankruptcy petition, although when the lienholder comes to prove his claim for the deficit for participation in dividends, his interest will be restricted to accruals at the date of the filing of the petition.⁴⁵

§ 1985½. Statutory Regulations of Party's Right to Maintain Suit, Not Binding.—Statutory regulations of a party's right to maintain suit, as, for example, that partnerships doing business under fictitious names or names not showing who are the members, shall not maintain suit until compliance with certain regulations, are not binding upon the bankruptcy court, for the federal courts will prescribe their own regulations of the right of a party, otherwise competent, to institute or maintain proceedings.⁴⁶

§ 1986. Separate Accounts of Each Fund to Be Kept.—Separate accounts should be kept of the proceeds of sale where liens are involved, all of which are not liens upon the entire property, so that the lienholders may have the means of determining what their respective rights are in the proceeds.⁴⁷

Keyser v. Wessel, 12 A. B. R. 127, 128 Fed. 281 (C. C. A. Pa., affirming *In re Smith*, 10 A. B. R. 586): "This case is plainly distinguishable from that of *Carroll & Bro. Co. v. Young*, 9 Am. B. R. 643, 119 Fed. 577, which was decided by this court about a year ago. In that case, the lien creditors had been prompt and persistent in asserting their rights. They had made timely objection to the property being sold divested of their liens, and had pointed out the very difficulty which was subsequently brought forward as a bar to their rights. In that case, as in this, it was too late to question the propriety of the order of sale which had been made; but it was not impossible, as it is in the present case, to determine the proportional value of the particular part bound by the liens to the gross purchase price, and hence the order which was there made, by which the distribution was opened to permit the lien creditors to prosecute their claims as such, was both just and practicable. We adhere to our decision in *Carroll & Bro. Co. v. Young*, but to the very different circumstances and situation disclosed by the record now before us it has no application."

In re Klapholz & Brien, 7 A. B. R. 703, 113 Fed. 1002 (D. C. Penn.): "The fund was produced by the sale of all the bankrupt's personal property, including the clothing manufactured by the claimant, clothing manufactured by other persons, and various other articles; and there is no evidence concerning the price for which the suits in question were sold. The claimant had notice

44. Analogously, *Knapp & Spencer v. Drew*, 20 A. B. R. 355, 160 Fed. 413 (C. C. A. Neb.).

45. *Coder v. Arts*, 18 A. B. R. 513, 152 Fed. 943 (C. C. A. Iowa), quoted at § 1147.

46. See ante, § 1894½; *In re Farmers Supply Co.*, 22 A. B. R. 460, 170 Fed.

502 (D. C. Ohio), quoted at § 1894½; *In re Stevens*, 23 A. B. R. 239, 173 Fed. 842 (D. C. Ore.), quoted at § 758½.

47. Inferentially and suggestively, *George Carroll & Bro. v. Young*, 9 A. B. R. 643, 119 Fed. 577 (C. C. A. Pa.); impliedly, *In re Gerry*, 7 A. B. R. 461, 112 Fed. 957 (D. C. Pa.).

of the sale, which was made by the receiver under an order of court and was afterwards duly confirmed without objection, and he should have asked the court to direct this clothing to be sold separately, in order that the fund thus produced might be earmarked and the validity of his claim upon it be considered. The court had no knowledge that he was asserting a lien for the manufacture of these goods, and, as they had passed out of his possession into the custody of the receiver, it was his duty to make seasonable claim to priority of payment. Otherwise, he must be held to have taken the risk that the goods might be sold in such a manner that the proceeds might be indistinguishably mingled with the proceeds of the other property of the bankrupt."

Obiter, In re Shoe & Leather Reporter, 12 A. B. R. 248, 129 Fed. 588 (C. C. A. Mass.): "While, of course, we would ordinarily expect the District Court, before selling property in lump as to which there are conflicting claims, to establish by proper inventory and appraisal the basis for a distribution of the proceeds when the title to the portions of the property in dispute is settled, yet his record presents nothing definite with regard to this proposition of the petitioners."

§ 1987. Failure to Object to Sale without Separation Waives Rights.—And the lienholder waives his rights by failure to object to a sale, where such separation of accounts is not kept.⁴⁸

Thus, where a landlord, entitled to priority under the state law for one year's rent out of the sale of a tenant's stock and fixtures, makes no objection to a sale or confirmation of a sale of the stock, fixtures and liquor license in bulk for a lump sum, the landlord's claim for priority of rent should be disallowed, because of the impossibility of determining how much were the proceeds of the stock and fixtures on which only the landlord has his lien.⁴⁹

Again, the owner of a municipality's claim for taxes upon two parcels of land, where the two were part of twelve parcels sold for a lump sum, he having notice thereof and not objecting thereto, has waived whatever rights he might have had had he required separation of the funds and payment from the proceeds of the parcels covered by his lien.⁵⁰ Likewise, where there was a lien upon a clothing stock and the clothing was sold together with the property, but no separate account was kept nor ordered kept, although the lienholder was notified, and nothing was known as to the separate price for which the clothing sold; the lienholder was held to have waived all right to payment.⁵¹

48. In re Klapholz & Brien, 7 A. B. R. 703, 113 Fed. 1002 (D. C. Pa.) quoted § 1986; In re Shoe & Leather Reporter, 12 A. B. R. 248, 250, 129 Fed. 588 (C. C. A. Mass.) quoted § 1986; In re Caldwell, 24 A. B. R. 495, 178 Fed. 377 (D. C. Ga.).

For a case where conditional vendor did not so fail, but protested, see In re Grainger, 20 A. B. R. 166, 160 Fed. 69 (C. C. A. Calif.); compare, In re Goldsmith, 21 A. B. R. 845, 168 Fed. 779 (D. C. N. Y.).

49. Keyser v. Wessell, 12 A. B. R.

126, 128 Fed. 281 (C. C. A. Penn., affirming In re Smith, 10 A. B. R. 586); Vollmer v. McFadgen, 20 A. B. R. 540, 161 Fed. 914 (C. C. A. Pa.); In re McFadgen, 19 A. B. R. 481, 156 Fed. 715 (D. C. Pa., affirmed sub nom. Vollmer v. McFadgen, 20 A. B. R. 540, 161 Fed. 914). But compare peculiar facts In re Varley & Bauman Co., 26 A. B. R. 104, 188 Fed. 761 (D. C. Ala.).

50. In re Gerry, 7 A. B. R. 461, 112 Fed. 957 (D. C. Pa.).

51. In re Klapholz & Brien, 7 A. B. R. 703, 113 Fed. 1002 (D. C. Penn.).

Similarly, a conditional vendor of chattels or other owner of interests therein who has consented to a sale of the property involved waives his right to the value of his specific property by failure to have separate account kept.

In re Great Western Mfg. Co., 18 A. B. R. 259, 152 Fed. 123 (C. C. A. Neb.): "One who acquiesces in a sale under an order of the court of his property and the estate of the bankrupt in one lot, and thereafter prays for a preference in payment out of the sale, is estopped from receiving a larger proportion of the proceeds than the value of his property bore to the value of the lot sold at the time of the sale."

But failure to file exceptions to a return of sale that did not separately state the several amounts realized for each fund out of the entire proceeds, does not waive objections to the original order to sell as an entirety and to the transfer of the liens to the fund, where the objections were made on the ground of the difficulty of separating the funds, the order of sale also providing that the sale was to be "without prejudice to the right of lien creditors to claim from the fund derived from said sale the amount of their respective liens."⁵²

If the lienholder actually is present at a sale made without separation, he waives any lack of notice to him by mail.⁵³

§ 1988. Taking Additional Evidence, after Sale, to Fix Proportions of Fund.—It would be proper for the referee, sua sponte, to take additional evidence as to the proportion of the funds respectively assignable to each lienholder, after the sale, if the sale were made as an entirety without arrangement for separation of the proceeds.⁵⁴

Obiter, Geo. Carroll & Bro. v. Young, 9 A. B. R. 647, 119 Fed. 577 (C. C. A. Pa.): "But, if the evidence on that point was incomplete, we think that the referee sua sponte should have taken additional proof to show the portion of the purchase price representing the building and its ground, apart from the machinery and other equipment."

§ 1989. Expenses of Preservation and Sale Paid Out of Particular Fund Involved.—The costs and expenses of the preservation of the property involved and of its sale are to be paid out of the particular fund derived from the sale of such property.⁵⁵

⁵². George Carroll & Bro. v. Young, 9 A. B. R. 643, 119 Fed. 577 (C. C. A. Pa.).

⁵³. In re Caldwell, 24 A. B. R. 495, 178 Fed. 377 (D. C. Ga.).

⁵⁴. In re Goldsmith, 21 A. B. R. 845, 168 Fed. 779 (D. C. N. Y.).

⁵⁵. In re Cogley, 5 A. B. R. 731, 107 Fed. 73 (D. C. Iowa); In re Prince & Walter, 12 A. B. R. 681, 131 Fed. 546 (D. C. Pa.). Compare, In re Tebo, 4 A. B. R. 235, 101 Fed. 419 (D. C. Va.), where the rule is stated even more broadly, and erroneously so. Im-

plied, In re Baughman, 20 A. B. R. 811, 163 Fed. 669 (D. C. S. Car.). But compare, apparently but not really, contra, Mills v. Virginia-Carolina Lumber Co., 20 A. B. R. 750, 164 Fed. 168 (C. C. A. N. Car.), quoted at § 1993; inferentially, In re Evans Lumber Co., 23 A. B. R. 881, 176 Fed. 643 (D. C. Ga.).

Compare post, § 1993. In re Howard, 31 A. B. R. 251, 207 Fed. 402 (D. C. N. Y.). To this general effect, perhaps, In re Chambersburg Mfg. Co., 26 A. B. R. 107, 190 Fed. 411 (D. C. Pa.).

In *re Utt*, 5 A. B. R. 383, 105 Fed. 758 (C. C. A. Ills.): "The mortgaged property having been sold by the trustee in bankruptcy under the order of the District Court, it is equitable and right that the expenses of the sale, including advertisement, appraisal, if appraisal was required by law, revenue stamps, and compensation to the trustee not exceeding that of the master in chancery if the sale had been made by him under the decree of the state court, should be paid out of the proceeds of the sale; but, in so far as it was directed that attorneys, the clerk and the marshal should be paid for services in the bankruptcy proceedings not directly connected with the sale, or in the suit for an injunction, the order made was without justification in law or equity. This includes the \$100 directed to be paid to the attorney for the trustee, for whose assistance, in connection with the sale, there could have been no necessity."

And this is so notwithstanding there be not enough left to pay the liens in full.⁵⁶

In *re Williams Estate (Anheuser-Busch Brew. Ass'n v. Harrison)* 19 A. B. R. 389, 156 Fed. 934 (C. C. A. Wash.): "It thus appears that all of the property of the bankrupt was covered by the brewing association's liens, and that the total amount realized from the sale of the property upon which the petitioner had valid liens was less than the amount of those liens. The real question for decision, therefore, is to what extent, if at all, funds realized by the sale of property upon which a creditor of a bankrupt has valid liens, proof of which secured claims is filed in the bankruptcy court after the making of such sale, and when the proceeds of the sale are insufficient to pay the liens in full, may be used to pay the general costs of administration of the bankrupt's estate. It is true that the record in the case shows that the lienholder voluntarily came into the bankruptcy court and asked that the property covered by its liens be sold by that court. The Bankruptcy Act * * * in terms declares that none of its provisions shall effect a valid lien. But the estate of a bankrupt is interested in any excess that may exist over and above the amount of such liens. So it was held by this court in the case entitled *In re Jersey Island Packing Co.*, 14 Am. B. R. 689, 138 Fed. 625, 627, 71 C. C. A. 75, 2 L. R. A. (N. S.) 560, that 'property on which there is a mortgage or other lien passes to the trustee in bankruptcy and is therefore in the custody of the court of bankruptcy,' and further, in the same case, that 'the provision of the Bankruptcy Act that such a lien shall not be affected by the bankruptcy proceedings has reference only to the validity of the lienholder's contract. It does not have reference to his remedy to enforce his rights. The remedy may be altered without impairing the obligation of his contract, so long as an equally efficient and adequate remedy is substituted.' By coming into the bankruptcy court, therefore, the holder of a valid lien upon the estate of a bankrupt comes into an appropriate place and into a court amply able to enforce and protect his rights. By doing so the lienholder waives none of his rights. The enforcement of his lien in another court would entail upon the proceeds of the property upon which the lien exists the payment of the appropriate court costs; and so, in the enforcement of such lien in a court of bankruptcy, the proceeds of the property of the bankrupt upon which such lien exists is properly chargeable with the costs of such court appropriate to such enforcement, but with no other or further costs."

⁵⁶ In *re Baughman*, 20 A. B. R. 811, 163 Fed. 669 (D. C. S. Car.), although the qualification is added that the lienholder did not object.

§ 1990. **Each Fund to Bear Its Own Expenses and Costs.**—And each fund is to bear its own expenses and costs.⁵⁷

In *re Cogley*, 5 A. B. R. 731, 107 Fed. 73 (D. C. Iowa): "It sometimes happens that lienholders desire to obtain a title from the trustee, either through a public sale made by him, or by a direct conveyance; and in such cases the trustee can generally obtain some small sum for conveying the title, which will enure to the benefit of the general creditors. * * * In the case at bar * * * the trustee carried through a sale for the benefit of the mortgagees saving them the costs of a foreclosure suit, and then paid the costs of this sale out of the money in his hands realized from the sale of assets on which the mortgagees had no lien whatever. If the creditors had excepted * * * the action * * * would be set aside as a clear error."

In *re Torchia*, 26 A. B. R. 188, 185 Fed. 576 (D. C. Pa.): "The referee was of the opinion that because the Bankruptcy Act provided that valid liens should not be affected and because as he found, there was no money in the hands of the trustee for distribution except the proceeds of the real estate, and because the liens thereon exceeded in amount the proceeds available thereto, therefore nothing could be applied to such commissions and counsel fees. Under the circumstances of this case I think the referee was in error."

"It is undoubted now that a court of bankruptcy has power to sell real estate discharged of liens after notice to lien creditors. From the earliest times a court of equity has assumed jurisdiction of the ascertainment of liens and of their enforcement by sale or otherwise, and of the distribution of the proceeds of sale among the lienors. It is proper in a case like the present, that the rights of those claiming to have a lien should be ascertained by the bankruptcy court. If referee's and trustee's fees are not to be paid out of the fund realized by the sale of real estate discharged of liens, there will be no incentive to the small creditor of himself to institute proceedings to determine the validity of liens. In this case, had the mechanics' liens, which are purely statutory, been determined to have been void, a large fund would have been applicable to the claims of the general creditors. They raised no question about the sale discharged of liens. They were benefited thereby. They were at no expense, as they would have been had they been permitted to enforce their liens themselves, and they ought in equity and good conscience be willing that the referee's and trustee's commissions and expenses should be allowed and paid out of the fund."

"Apart from that, however, it is the undoubted rule that the expenses of creating a fund should be paid out of it. The expenses in such case should include also reasonable compensation to the parties who have been instrumental in creating the fund."

"While liens cannot be affected by the Bankruptcy Act, they are not thereby given a higher status than they had before the act was passed. In Pennsylvania, under the laws regulating assignments for the benefit of creditors, by Act of February 17, 1876 (P. L. 4), a public sale, and by Act May 24, 1893 (P. L. 128), a private sale, of real estate might be ordered free and discharged of all other liens except the liens of mortgages. Also a public sale with like effect might be ordered by virtue of section 19 of Insolvency Act of 1901 (P. L. 415). In that State also the orphan's court may order a sale of a decedent's real estate, unless for payment of debts, with the same result, but with

⁵⁷. Impliedly, In *re Morris*, 19 A. B. R. 781, 156 Fed. 597 (D. C. Pa.); In *re Stew-art*, 27 A. B. R. 529, 193 Fed. 791 (D. C. La.).

the same limitation. When such a sale under either of the statutory powers thus mentioned has been had, it has never been doubted that the commissions of the assignee, or administrator, as the case may be, and his counsel fees are payable out of the fund before distribution to judgment or mechanics' liens."

And the Amendment of 1910 did not alter the law in this respect but was simply declaratory of it.

Obiter, In *re Torchia*, 26 A. B. R. 1888, 185 Fed. 576 (D. C. Pa.): "If the Bankruptcy Act of 1898 be not in its provisions with respect to the compensation to trustees where the assets to be administered have been derived from the sale of property subject to liens, it has been made specially so by the amendment of June 25, 1910 (chapter 412, 36 Stat. 840), which provides, in section 9, that trustees shall receive 'commissions on all moneys disbursed or turned over to any person including lienholders.' I cannot escape the conclusion that the provision last quoted is declaratory of the law as it was."

Of course, where the expenses of preservation cover several funds, they may be apportioned among the various funds.⁵⁸

§ 1991. Proportionate Part Not to Be Charged against Each Lien.—A proportionate part of the expenses, etc., are not to be charged against each lien in accordance with its share of the proceeds;⁵⁹ although where the lien is only on part, the expenses assignable to that part, of course, may be arrived at proportionately.⁶⁰

But, of course, where the expenses are jointly incurred in the protection of several different funds, they may be apportioned among the various funds.⁶¹

§ 1992. Costs and Expenses First Deducted and Liens Paid Out of Remainder.—The costs and expenses are first in the order of priority in such sales; and are to be first deducted, and the liens are to be paid out of the remainder, in the order of their priority.⁶² Thus, costs, expenses and taxes have precedence over dower.⁶³ Likewise costs and expenses of

58. Instance, In *re Evans Lumber Co.*, 23 A. B. R. 881, 176 Fed. 643 (D. C. Ga.).

59. *McNair v. McIntyre*, 7 A. B. R. 638, 113 Fed. 113 (C. C. A. N. C., reversing In *re Sanderlin*, 6 A. B. R. 384, 109 Fed. 857, D. C. N. C.); *Mills v. Virginia-Carolina Lumber Co.*, 20 A. B. R. 750, 164 Fed. 168 (C. C. A. N. C.), quoted at § 1993.

60. In *re Davis*, 19 A. B. R. 98, 155 Fed. 671 (D. C. N. Y.); In *re Holmes Lumber Co.*, 26 A. B. R. 119, 189 Fed. 178 (D. C. Ala.), criticized, however, as to other points in § 1971.

61. Instance, In *re Evans Lumber Co.*, 23 A. B. R. 881, 176 Fed. 643 (D. C. Ga.).

62. *McNair v. McIntyre*, 7 A. B. R. 638, 113 Fed. 113 (C. C. A. N. C.); In

re Prince & Walter, 12 A. B. R. 681, 131 Fed. 546 (D. C. Pa.) impliedly; In *re Baughman*, 20 A. B. R. 811, 163 Fed. 669 (D. C. S. Car.) impliedly. In *re Alaska Fishing, etc., Co.*, 21 A. B. R. 685, 167 Fed. 875 (D. C. Wash.); impliedly, In *re Allert*, 23 A. B. R. 101, 173 Fed. 733 (D. C. W. Va.); In *re Torchia*, 26 A. B. R. 579, 188 Fed. 207 (C. C. A. Pa.).

In *re Chambersburg Silk Mfg. Co.*, 26 A. B. R. 107, 190 Fed. 411 (D. C. Pa.), although in this case the court thought proper to state that the sale had been encouraged by the lienholders.

63. In *re Forbes*, 7 A. B. R. 42 (Ref. Ohio). See, also, cases cited under § 1989.

the sale have precedence over landlord's liens for rent.⁶⁴ Receiver's certificates have thus been given priority in certain cases.⁶⁵ Priority creditors are not entitled to come before lienholders:⁶⁶ the prior lienholder is entitled to be paid in full, after deduction of the costs and expenses, if the fund is sufficient.⁶⁷

§ 1993. General Costs of Administration Not Chargeable.—Only the costs and expenses of the sale of the particular property may be taxed against the fund: general costs of administration may not be so charged.⁶⁸

In *re Williams* (Anheuser Busch Brew. Asso. *v.* Harrison), 19 A. B. R. 389, 156 Fed. 934 (C. C. A. Wash.): "They are not chargeable with the general costs of the administration of the bankrupt's estate, such as the services of a receiver in carrying on the business of the bankrupt, the expenses and losses of such business, the fees of the attorney for such receiver, the general fees of the trustee or those of his attorney. If so, the valid lien upon the estate of the bankrupt, which the Bankruptcy Act expressly declares shall be unaffected by any of its provisions, might very readily be destroyed, as it would unquestionably be, should such costs equal or exceed the proceeds in cases like the present, where the aggregate amount of the valid liens exceeds the proceeds of the entire estate of the bankrupt." Quoted further at § 1989.

Mills v. Virginia-Carolina Lumber Co., 20 A. B. R. 750, 164 Fed. 168 (C. C. A. N. Car.): "Whilst we think, therefore, that the judgment of the District Court, allowing the proof of the \$750.00 debt, should be affirmed, we feel constrained to modify the judgment with respect to cost. In the order which was filed by the District Court from the report of the referee, we find the following: 'It is further ordered and adjudged that as the creditor (meaning the Virginia-Carolina Lumber Company) voluntarily came into court and filed its claim for allowance, that said claim must bear its pro rata part of the costs of the administration under the proceedings in bankruptcy.' Aside from the mere costs incident to the proof of the claim, we do not see how this creditor should be required to pay any part of the costs of the administration of this bankrupt's estate. The lumber company had its claim secured by deed in trust on the property of the bankrupt and it was entitled to have its claim paid in full, provided the property so conveyed would bring enough. The trustee in bankruptcy elected to sell this property and has the proceeds of the sale in hand. The lumber company, in our opinion, is entitled to have of the proceeds of the sale sufficient to pay its debt and interest, provided there is enough.

64. In *re Morris*, 19 A. B. R. 781, 156 Fed. 597 (D. C. Pa.).

65. In *re Alaska Fishing, etc., Co.*, 21 A. B. R. 685, 167 Fed. 875 (D. C. Wash.).

66. In *re Allert*, 23 A. B. R. 101, 173 Fed. 691 (D. C. N. Y.). See post, § 2186; also, see In *re Proudfoot*, 23 A. B. R. 106, 173 Fed. 733 (D. C. W. Va.).

67. In *re Allert*, 23 A. B. R. 101, 173 Fed. 691 (D. C. N. Y.).

68. Compare post, § 2010. In *re Stewart*, 27 A. B. R. 529, 193 Fed. 791 (D. C. La.); In *re Zehner*, 27 A. B. R. 536, 193 Fed. 787 (D. C. La.); In *re Morris*, 19 A. B. R. 781, 156 Fed. 597 (D. C. Pa.); In *re Utt*, 5 A. B. R. 383, 105 Fed.

754 (C. C. A. Ills.); In *re Frick*, 1 A. B. R. 719 (Ref. Ohio); *Stewart v. Platt*, 101 U. S. 731; In *re Goldville Mfg. Co.*, 10 A. B. R. 552, 118 Fed. 892 (D. C. S. C.).

But compare, In *re Allison Lumber Co.*, 14 A. B. R. 78, 137 Fed. 643 (D. C. Ga.).

Contra. In *re Tebo*, 4 A. B. R. 250, 101 Fed. 419 (D. C. W. Va.). Contra, as to petitioning creditor's attorney fees, In *re Erie Lumber Co.*, 17 A. B. R. 700, 150 Fed. 817 (D. C. Ga.). But this case on the facts is reconcilable with the rule, since the petitioning creditor's attorney helped preserve the fund.

If the property did not bring enough to pay the debt and interest in full, then the lumber company is entitled to have the whole of the proceeds. In other words, this creditor, which has simply come into a bankruptcy court and established a debt that is a lien upon specific property of the bankrupt, should not be charged so as to reduce the security by making the fund arising from such specific property liable for the costs of the general administration of the bankrupt's estate."

In *re Howard*, 31 A. B. R. 251, 207 Fed. 402 (D. C. N. Y.): "The bankruptcy court cannot order mortgaged premises sold free and clear of the lien of the mortgage and use the proceeds of said sale, properly applicable to the payment of the mortgage, to pay the general expenses of administering the estate in bankruptcy, but I do not doubt its power to order and make a sale free and clear of the mortgage, bring the proceeds into court, ascertain the amount actually due and owing on the bond and mortgage, and make proper allowance for the necessary expenses of so doing."

In *re Prince & Walter*, 12 A. B. R. 681, 131 Fed. 546 (D. C. Pa.): "A sale of the property free of liens may undoubtedly be ordered, but, if this is done, the proceeds must be applied to their satisfaction, undiminished by anything except the costs of sale, or the expenses, if any, which have been undertaken for, and result to, their benefit. They are not concerned with the bankruptcy proceedings outside of this, and cannot, therefore, be charged with the cost of instituting them or carrying them on."

In *re Clark Coal & Coke Co.*, 23 A. B. R. 273, 173 Fed. 658, 176 Fed. 955 (D. C. Pa.): "But that with this slight power [Bankr. Act, § 2 (5)], and in the face of § 67d, 'that liens given or accepted in good faith should not be affected by the act,' a court of bankruptcy, without notice, can take the money of a lien creditor to pay the expenses of the general estate, or provide a fund for distribution among the general creditors, does not appear to us to be sound." [Quoted further at § 1996. Also, see opinion of referee in 22 A. B. R. 843, 57 Pitts. L. J. 205.]

But even the expenses of a receiver in the state court may be charged against the fund of the secured creditor, if such fund benefited thereby.⁶⁹

In *re Vulcan F'dy & Mach. Co.*, 24 A. B. R. 825, 180 Fed. 671 (C. C. A. Pa.): "Lienholders are, therefore, the virtual owners of the property pro tanto, and (as a general proposition) this substantial ownership is not to be disturbed without their consent. The Pennsylvania cases also regard the holders of liens as owners of a real, although an equitable, interest in the property, and their rights in that character are carefully guarded. *Bowman's Appeal*, 90 Penn. 178; *Burkholder's Appeal*, 94 Penn. 522; *Wolf's Appeal*, 106 Penn. 545 (where lien creditors of an assignor are spoken of as 'substantial owners of his real estate'). It is no doubt true that the Federal tribunals support the power of the District Court to sell a bankrupt's real estate discharged of liens—and to that extent the position of a lien is undoubtedly affected—but care is always taken to protect the liens by transferring them to the fund produced by the sale, and their virtual ownership of the property is thus effectively admitted. It is also true that in some cases certain expenses have been charged against lienholders, for example, the expense of selling the encumbered property, and such a charge may no doubt be warranted under some conditions. It would certainly be warranted if the lienholders came into the District Court (as they did in several reported cases) and asked that the sale might be made by that

69. In *re Allison Lumber Co.*, 14 A. B. R. 78, 137 Fed. 643 (D. C. Ga.).

tribunal, for otherwise they would themselves be put to a similar expense in proceeding upon their liens in another forum. But where it is sought to charge a lienholder with the cost of preserving and administering the encumbered property, as distinguished from the cost of its sale, it becomes necessary to consider the particular situation with great care, paying due regard to the rights of those who are in equity part owners of the property, for they cannot be deprived of their valuable except in strict accordance with legal or equitable rules. Especially is this true when a lienholder stands upon his lawful rights, and does not assent, expressly or by necessary implication, to the acts for which he is afterwards asked to pay. To make such charges a prior lien upon the fund produced by a sale, in effect compels an owner to pay for what he has never ordered—may indeed have strenuously opposed—and, under the guise of protecting his interests, may perhaps impair them seriously. Bankruptcy proceedings take place in a court of equity, and it should always be remembered that holders of valid liens have a statutory right to preferred treatment. If the receiver or trustee has a reasonable belief that the property is worth substantially more than the liens, it may no doubt be his duty to preserve this equity for the general creditors. But—speaking generally—since such steps as may be taken for this purpose are in the interest of these creditors, the cost should be paid by them and not by the lienholders—whose debts, indeed, are often perfectly secure, and receive no benefit from such effort as may be made to turn the equity into cash. We do not attempt to lay down a general rule to cover all cases. This would obviously be impracticable, but we think it is safe to say that the holders of liens are ordinarily entitled to judge for themselves what their interests may require, and that these interests cannot be affected without their consent in the effort to benefit persons whose rights are inferior to their own. We agree with the appellants' counsel that there is a plain analogy between a situation like this and the case in which it has been held that mortgage creditors of a private corporation should not have their security displaced by receiver's certificates, unless, perhaps, under extraordinary circumstances."

§ 1994. Trustee's Attorney's Fees and Expenses Benefiting Entire Fund Chargeable but Not for Services in Litigating Liens.—The trustee's attorney's fees and other expenses incurred in behalf of the entire fund are chargeable against the fund, even to the loss of the lienholder, but the fees for contesting liens in behalf of general creditors are not chargeable against the fund but against the general creditors, to be paid for out of the general estate.⁷⁰

§ 1995. Referee Has Authority to Tax Costs and Expenses.—The referee has authority to tax the costs and expenses.⁷¹

70. In re Waterloo Organ Co., 17 A. B. R. 312, 147 Fed. 814 (D. C. N. Y.); In re Williams (Anheuser-Busch Brew. Assn. v. Harrison), 19 A. B. R. 389, 156 Fed. 934 (C. C. A. Wash.), quoted at §§ 1993, 1989; In re Howard, 31 A. B. R. 264, 207 Fed. 402 (D. C. N. Y.); In re Freeman, 27 A. B. R. 16, 190 Fed. 48 (D. C. Ga.); In re Torchia, 26 A. B. R. 579, 188 Fed. 207 (C. C. A. Pa.).

71. In re Scott, 7 A. B. R. 710 (Ref.

Mass.); Inferentially, In re Todd, 6 A. B. R. 88, 109 Fed. 265 (D. C. N. Y.); In re Torchia, 26 A. B. R. 188, 185 Fed. 576 (D. C. Pa.), quoted at § 1990. To the same effect, In re Rome, 19 A. B. R. 820, 162 Fed. 971 (D. C. N. J.).

Where a secured creditor is given the regular ten days' notice by mail of the proposed sale of the property covered by his security free from liens and neglects to protest at the time set for the hearing of the application and

§ 1996. Costs and Expenses Taxable.—The costs and expenses generally taxable are as follows: the expense of publishing or advertising the sale;⁷² of abstract and insurance,⁷³ if necessary;⁷⁴ expense of referee in sending the notices of sale required by law to be sent; appraiser's fees for appraisal of the property sold; trustee's⁷⁵ expenses in caring for the property involved.⁷⁶

But the expenses of continuing the business for the benefit of general creditors may not be charged against the fund to the detriment of a good and valid lien thereon, where the lienor did not participate nor consent.⁷⁷

In *re Clark Coal & Coke Co.*, 23 A. B. R. 273, 173 Fed. 658, 176 Fed. 955 (D. C. Pa.): "Unless the lien creditor came into court, or was brought into court by regular process, and consented to the operation of the plant, or unless the facts would warrant the conclusion that it was under such circumstances as would estop the lien creditor that the business was continued, the lien creditor could not be displaced and the property covered by his lien swept away from him." [Quoted further at § 1993.]

Expense of the trustee for attorneys' fees in filing the petition for leave to sell, for examining the abstract, getting the parties into court, and for other services redounding to the general benefit of the fund are chargeable, as a first lien, on the fund;⁷⁸ but not attorney's fees for other services.⁷⁹

And there can be no allowance therefrom for the bankrupt's nor the

afterwards seeks to take advantage of the fact that the sale reduced his security, all the costs will be taxed against him. In *re Goldsmith*, 9 A. B. R. 419, 118 Fed. 763 (D. C. Tex.).

72. In *re Prince & Walter*, 12 A. B. R. 681, 131 Fed. 546 (D. C. Pa.); In *re Utt*, 5 A. B. R. 383, 105 Fed. 754 (C. C. A. Ills.); In *re Morris*, 19 A. B. R. 781, 156 Fed. 597 (D. C. Pa.); instance, In *re Chambersburg Mfg. Co.*, 26 A. B. R. 107, 190 Fed. 411 (D. C. Pa.).

73. In *re Holmes Lumber Co.*, 26 A. B. R. 119, 189 Fed. 178 (D. C. Ala.).

But insurance on the property incurred really for the benefit of general creditors who are hoping that by a sale enough may be realized to afford a surplus has been denied a place in the charge against the mortgaged fund, In *re Vulcan F'dy & Mach. Co.*, 24 A. B. R. 825, 180 Fed. 671 (C. C. A. Pa.); but it is submitted that the test should not be the "motive" of the trustee.

74. In *re Prince & Walter*, 12 A. B. R. 681, 131 Fed. 546 (D. C. Pa.).

As to insurance compare, where refused, In *re Vulcan F'dy & Mach. Co.*, 24 A. B. R. 825, 180 Fed. 671 (C. C. A. Pa.).

75. In *re Utt*, 5 A. B. R. 383, 105 Fed. 754 (C. C. A. Ills.); In *re Morris*, 19 A. B. R. 781, 156 Fed. 597 (D. C. Pa.).

Appraiser's Fees.—See post, § 2121.

76. Expense of running a hotel pending sale, allowed. In *re Prince & Walter*, 12 A. B. R. 681, 131 Fed. 546 (D. C. Pa.); watchman's pay and wages of clerk at sale; In *re Morris*, 19 A. B. R. 781, 156 Fed. 597 (D. C. Pa.); watchman's pay, In *re Chambersburg Mfg. Co.*, 26 A. B. R. 107, 190 Fed. 411 (D. C. Pa.); watchman's pay refused, In *re Vulcan F'dy & Mach. Co.*, 24 A. B. R. 825, 180 Fed. 671 (C. C. A. Pa.).

77. In *re Bourlier Cornice & Roofing Co.*, 13 A. B. R. 585, 133 Fed. 958 (D. C. Ky.). Compare, In *re Williams* (Anheuser-Busch Brew. Assn. *v.* Harrison), 19 A. B. R. 389, 156 Fed. 934 (C. C. A. Wash.), quoted at §§ 1989, 1993.

78. Inferentially, In *re Utt*, 5 A. B. R. 383, 105 Fed. 754 (C. C. A. Ills.); In *re Morris*, 19 A. B. R. 781, 156 Fed. 597 (D. C. Pa.); Impliedly, In *re Torchia*, 26 A. B. R. 188, 185 Fed. 576 (D. C. Pa.), quoted on other points at § 1990. For collecting insurance on the premises, In *re Holmes Lumber Co.*, 26 A. B. R. 119, 189 Fed. 178 (D. C. Ala.).

79. In *re Utt*, 5 A. B. R. 383, 105 Fed. 754 (C. C. A. Ills.); In *re Waterloo Organ Co.*, 9 A. B. R. 427, 118 Fed. 904 (D. C. N. Y.).

petitioning creditors' attorneys' fees not connected with the direct preservation of the property sold.⁸⁰

Liddon & Bro. v. Smith, 14 A. B. R. 204, 135 Fed. 43 (C. C. A. Fla.): "It seems manifest to us that the services rendered by the attorney J. M. Calhoun, nominally for the bankrupt, had no legitimate connection with the preservation of the estate, and that under the conditions existing it would be most inequitable to allow his account for fees therefor, to take rank of the mortgagee's claim as a charge against the proceeds of the sale of the mortgaged property."

Nor for services performed by the trustee's attorney in behalf of general creditors in endeavoring to defeat liens, etc.;⁸¹ except that, where the fund actually is insufficient even to pay the lienholders, it is perhaps permissible to charge against the fund the services of the trustee's attorney in defeating improper claims for liens thereon.

Perhaps, *In re Waterloo Organ Co.*, 18 A. B. R. 752, 154 Fed. 657 (C. C. A. N. Y.): "The trustee in bankruptcy presents a bill for services and attorney's fees in the controversy (which was heretofore brought up to this court) as to the validity of the two bonds held by Bacon and the 21 bonds held by the bank. That litigation was not a frivolous one, as our former opinions indicated, and since its object was to reduce the number of claimants upon the special fund belonging primarily to the secured (mortgage) creditors, that fund is the proper one to bear the expense."

Nor for a mortgagee's attorney, even in states where it is legal to stipulate for attorney's fees on foreclosure, if the mortgage only provides therefor in the event of "foreclosure."⁸²

^{80.} *In re Goldville Mfg. Co.*, 10 A. B. R. 552, 118 Fed. 892 (D. C. S. C.); *In re Frick*, 1 A. B. R. 719 (Ref. Ohio). To similar effect, *In re Prince & Walter*, 12 A. B. R. 681, 131 Fed. 546 (D. C. Pa.); *contra*, *In re Meis*, 18 A. B. R. 704 (Ref. Ky.). Apparently, *contra*, *In re Erie Lumber Co.*, 17 A. B. R. 770, 150 Fed. 817 (D. C. Ga.): But this case may be reconciled with the rule on its facts for there the petitioning creditors' attorneys had aided in the preservation of the fund. Apparently, *contra*, *In re Duncan*, 2 A. B. R. 321 (D. C. Tex.): But this case states no reasons and is not to be considered of much weight.

^{81.} See ante, § 1994.

^{82.} But compare, *In re Waterloo Organ Co.*, 17 A. B. R. 300, 147 Fed. 814 (D. C. N. Y.), where a trustee for mortgage bondholders was allowed compensation and attorney's fees; compare *Chestertown Bank v. Walker*, 20 A. B. R. 840, 163 Fed. 510 (C. C. A. Md.).

Also compare, *In re Claussen*, 21 A. B. R. 34, 164 Fed. 300 (D. C. S. Car.),

wherein mortgagee's attorney refused compensation for services rendered exclusively for mortgagee's benefit, but apparently would have been allowed for services for general benefit. Compare, *In re Blanchard Shingle Co.*, 21 A. B. R. 142, 164 Fed. 311 (C. C. A. Wash.), where a mortgagee was refused his attorney's lien for instituting foreclosure before bankruptcy, though the fee was allowed as a general claim.

Compare, *In re Wendel*, 18 A. B. R. 665, 152 Fed. 672 (D. C. Pa.); *In re Allert*, 23 A. B. R. 101, 173 Fed. 691 (D. C. N. Y.), wherein the attorney for a second mortgagee was refused compensation.

But compare perhaps a different rule where the mortgagee had applied for and been refused leave to start foreclosure suit, *In re Holmes Lumber Co.*, 26 A. B. R. 119, 189 Fed. 178 (D. C. Ala.); although this distinction probably should not prevail, since it would be a question, rather, as to the actual services performed and the validity under state law of such a provision as against the usury laws.

In *re Roche*, 4 A. B. R. 369, 101 Fed. 956 (C. C. A. Tex.): "The fees, to become a charge against the debtor or his property, must mature according to the contract of the parties. It follows that if the attorney's fees in this case became payable only upon the foreclosure of the trust deed by suit in the usual form, as by bill in equity, or, according to the practice in Texas, by petition praying for a foreclosure, with all parties claiming adversely before the court, they would not be collectible in a proceeding where the trustee in bankruptcy had sold the property and distributed the proceeds, although the same end might have been attained in securing the payment of the debt of the mortgagee. In other words, although the one proceeding might have been the equivalent of the other, and accomplished the same purpose, still the attorney's fees could only be recoverable upon the happening of the very contingency as to which the parties had contracted."

But attorney's fees have been allowed to mortgagees in sales in bankruptcy where proper by state law as part of the lien contracted for and not merely for "foreclosure."⁸³

Thus, even for services in opposing the adjudication in bankruptcy of the debtor, in a case where there was a trustee in a mortgage given to secure bondholders, who contested the adjudication in the interest of the bondholders.⁸⁴

And the statutory lien of the plaintiff's attorney for fees on foreclosure of a mechanics' lien is to be recognized in bankruptcy, and the trustee may not make a settlement in disregard thereof.⁸⁵

It has been held that in general the expenses and costs chargeable against a particular fund should not exceed what would have been chargeable had foreclosure in the state court been had,⁸⁶ but certainly there can be no hard and fast rule to such effect, though economy of administration should continually be borne in mind in this particular as in every other particular in bankruptcy.

Receiver's certificates for expenses in the preservation of the property involved are also chargeable.⁸⁷

Commissions of the referee, one per cent. on the amount realized over and above the expenses, are properly chargeable.⁸⁸ Likewise, commissions

83. In *re Wendel*, 18 A. B. R. 665, 152 Fed. 672 (D. C. Pa.), wherein the court reduced the amount from that stipulated for, in accordance with State law; also, see In *re Waterloo Organ Co.*, 17 A. B. R. 300, 147 Fed. 814 (D. C. N. Y.), and same case, modified by appellate court in 18 A. B. R. 752, 154 Fed. 657 (C. C. A. N. Y.), wherein a trustee for mortgage bondholders was allowed compensation and attorney's fees.

As where the mortgage provided therefor in case legal services became necessary to protect its interests, In *re Holmes Lumber Co.*, 26 A. B. R. 119, 189 Fed. 178 (D. C. Ala.); In *re Fabocher*, 27 A. B. R. 534, 193 Fed. 556 (D.

C. La.), although in this case the fees were not allowed at the sum stipulated for but rather at what the court determined to be "reasonable" fees.

Compare [allowance refused for lack of any evidence of value of services], In *re Torchia*, 26 A. B. R. 188, 185 Fed. 576 (D. C. Pa.).

84. In *re Waterloo Organ Co.*, 18 A. B. R. 752, 154 Fed. 657 (C. C. A. N. Y.).

85. In *re Adamo*, 18 A. B. R. 180, 151 Fed. 716 (D. C. N. Y.).

86. In *re Davis*, 19 A. B. R. 98, 155 Fed. 671 (D. C. N. Y.).

87. In *re Alaska Fish, etc., Co.*, 21 A. B. R. 685, 167 Fed. 875 (D. C. Wash.). Compare, also, ante, § 389.

88. Compare, however, In *re Morris*,

of the trustee,⁸⁹ which may be allowed in such sums as the court may deem right, but not to exceed the statutory rate of six per cent. on the first five hundred dollars, four per cent. on the next thousand, two per cent. on all over fifteen hundred dollars and less than ten thousand dollars and one per cent. on all above ten thousand dollars. And the trustee's commissions, according to the better practice, should not be allowed in excess of the compensation that would have been allowed a master in chancery had the sale been made by him under decree of the state court.⁹⁰ But the six per cent., etc., must not twice be computed, once on the first \$500 of the special fund and again on the first \$500 of the general fund.

Receiver's compensation for the care and preservation of the property sold is also entitled to priority as costs.⁹¹ By the Amendment of 1910 such compensation is to be by way of commissions.⁹² But the Amendment of 1910 is only declaratory of the law as it stood before with regard to the right to charge commissions of the referee, receiver and trustee out of the proceeds of sale.⁹³

Before the Amendment of 1910 there was a line of cases which denied commissions to the referee and trustee out of the fund until after the lien had been satisfied in full except where the lien was disputed or the lienholder himself had invoked the aid of the bankruptcy court;⁹⁴ but such ruling was to be criticised on the ground that it threw the peril of realizing upon encumbered property in bankruptcy (and most property in bankruptcy is encumbered) upon the trustee, virtually paralyzing his efforts and compelling him to perform services and to incur expenses at his own risk, even though he acted in the best faith. Such rule cannot be right in principle and necessarily must be unsound on analysis. The enunciation of the rule occurred usually in cases where there had been an abuse of discretion in ordering a sale clear and free of liens when there should have been ordered an abandonment or a sale subject to liens; but it is submitted that since that abuse of discretion was the real wrong perpetrated the correction should have been applied to such abuse—properly the order of sale should have been reviewed, or, perhaps, in extreme cases, the commissions of the referee or trustee, if in collusion, might be withheld for abuse of discretion and of the process of the court.

19 A. B. R. 781, 156 Fed. 597 (D. C. Pa.); *In re Baughman*, 20 A. B. R. 811, 163 Fed. 669 (D. C. S. Car.); *In re Torchia*, 26 A. B. R. 188, 185 Fed. 576 (D. C. Pa.), quoted at § 1990.

⁸⁹ *In re Morris*, 19 A. B. R. 781, 156 Fed. 597 (D. C. Pa.); *In re Baughman*, 20 A. B. R. 811, 163 Fed. 669 (D. C. S. Car.); *In re Torchia*, 26 A. B. R. 188, 185 Fed. 576 (D. C. Pa.), quoted at § 1990.

⁹⁰ Impliedly, *In re Utt*, 5 A. B. R. 383, 105 Fed. 754 (C. C. A. Ills.); *In re Stewart*, 27 A. B. R. 529, 193 Fed. 791

(D. C. La.); *In re Zehner*, 27 A. B. R. 536, 193 Fed. 787 (D. C. La.).

⁹¹ *In re Alaska Fish, etc., Co.*, 21 A. B. R. 685, 167 Fed. 875 (D. C. Wash.); *In re Torchia*, 26 A. B. R. 188, 185 Fed. 576 (D. C. Pa.), quoted at § 1990.

⁹² Bankr. Act, 48d and e. Also, see post, § 2118, et seq.

⁹³ *In re Torchia*, 26 A. B. R. 188, 185 Fed. 576 (D. C. Pa.), quoted at § 1990.

⁹⁴ See post, § 2104; also see *In re Harrison*, 24 A. B. R. 715, 179 Fed. 490 (C. C. A. Mo.).

It was held in one case that the Amendment, however, is not applicable to cases where the property brings "largely less" than the concededly valid encumbrances, on the doctrine that such deficiency was itself *prima facie* proof that the bankruptcy court had not "rightfully exercised its jurisdiction to sell free from liens;"⁹⁵ but it would seem that the objection to such sale should have been made by the lienholder at the outset, when first summoned into court, and that his failure to object before the sale was itself rather *prima facie* proof, or at any rate an admission by the lienholder, that the sufficiency or insufficiency of the price likely to be obtained was so entirely unknown and unascertainable that it would be a proper exercise of the bankruptcy court's jurisdiction to order a sale. Manifestly the proper time to object to the exercise of the jurisdiction to sell free of liens is the time such a sale is ordered; and the fact that the underlying motive of the trustee was not to protect the property for lienholders but rather to enable creditors to get any possible surplus, is not the test of the propriety of the charge.⁹⁶

§ 1997. Lienholder as Purchaser, May Apply Lien on Price, Except as to Superior Liens.—Where the purchaser is one of the lienholders, he may apply the value of his lien upon the purchase price, except, of course, as to costs and liens superior to his own; and his receipt should be accepted as part payment.⁹⁷

In *re Harrison*, 24 A. B. R. 715, 179 Fed. 490 (C. C. A. Mo.): "The creditor was entitled to have the purchase price credited on his allowed claim. It would have been a useless ceremony for him to pay the \$1,500 into court and then have it repaid him after credit on his allowed claim."

§ 1997½. Interest.—Where the funds are ample, interest on the lien

⁹⁵. In *re Holmes Lumber Co.*, 26 A. B. R. 119, 189 Fed. 178 (D. C. Ala.).

⁹⁶. But compare, apparently contra argument, In *re Vulcan F'dy & Mach. Co.*, 24 A. B. R. 825, 180 Fed. 671 (C. C. A. Pa.): "The referee and the court seem to have been misled by supposing that the trustee was acting in the interest of the lienholders when he employed a watchman, paid for insurance and incurred similar expenses. But he had no authority from the lienholders to spend any money on their behalf, and it is abundantly evident that he was solely considering the contingent interest of the general creditors, and was hoping to realize something from them. The experiment was to be for their benefit, and it is only just that they should pay for it. No doubt much of the money paid out by the trustee was of advantage to both mortgagees, but we do not see upon what ground these virtual owners can properly be asked to pay for what they did not authorize, expressly or by necessary im-

plication. No doubt they would have been obliged to protect the property at their own expense if it had been abandoned by the trustee, but this situation did not arise and need not be considered."

⁹⁷. In *re Waterloo Organ Co.*, 9 A. B. R. 427, 118 Fed. 904 (D. C. N. Y.); In *re Saxton Furnace Co.*, 14 A. B. R. 483, 136 Fed. 697 (D. C. Pa.); In *re Fayetteville, etc., Co.*, 28 A. B. R. 307, 197 Fed. 180 (D. C. Ark.).

But lienholders purchasing in the mortgaged property at foreclosure sale can not require that the rents collected therefrom by the trustee in the meantime be used in reimbursing him for taxes paid by him that are a lien at the time of purchase; In *re Hollenfeltz*, 2 A. B. R. 499, 94 Fed. 629 (D. C. Iowa).

Lienholder Bidder Charged More Expenses than Stipulated for in Order of Sale.—In one case a lienholder, second in priority who had bid in the property under an order of sale stipu-

is to be computed to date, and not merely to the time of the filing of the bankruptcy petition.⁹⁸

Coder v. Arts, 213 U. S. 223, 22 A. B. R. 1: "Nor do we think the circuit court of appeals erred in holding that, inasmuch as the estate was ample for that purpose, Arts was entitled to interest on his mortgage debt."

In re Torchia, 26 A. B. R. 188, 185 Fed. 576 (D. C. Pa.): "Ninth Question: 'Whether or not interest should be allowed on the various liens to the respective dates of sales, confirmations of sales, or to October 1, 1910.' The referee has assumed that October 1, 1910, would be the date when the payments would be made; but such date appears to have been arbitrarily selected and is not material to the ninth question. Interest is payable on the Kaufman mortgage to the date of payment of principal because the mortgage could not have been discharged by virtue of any of the Pennsylvania statutes above referred to. Interest is not payable upon the mechanics' liens or judgments to the date of payment of their principal sums, because they may be discharged by a judicial sale."

Nor merely to the time of the approval of the sale.⁹⁹

However, such rule only applies as to payments out of the fund covered by the lien. When the deficit is presented for allowance against the general estate for sharing in dividends, the amount of such deficit is to be arrived at by computing interest only to the date of the filing of the bankruptcy petition; otherwise, the mere existence of some security, however small, would produce inequality in the allowance of claims for sharing in dividends.

§ 1998. Trustee's Deed or Bill of Sale.—No form for a deed or bill of sale by the trustee has been prescribed. In general the deed should follow the analogy of assignee's, receiver's or administrator's deeds as prescribed by local statute or custom.¹

§ 1999. Remedies against Purchaser.—Where the purchaser defaults in payment there are several different remedies available, dependent on the facts of the case.

Among other remedies, the trustee may resell and charge the purchaser with the difference.²

The purchaser is chargeable with interest from the date of the confirmation of the sale until he makes payment.³

lating that, if he bid it in, he should have to stand only \$500 of expenses, was charged \$4454.11 of expenses, the appellate court reversed the lower court, *In re Vulcan F'dy & Mach. Co.*, 24 A. B. R. 825, 180 Fed. 671 (C. C. A. Pa.). But see dissenting opinion.

Creditor, as Purchaser, Applying Dividend on Purchase Price.—Similarly, a creditor, as a purchaser, may doubtless apply his dividend on the purchase price, obiter, *In re Cornell Co.*, 26 A. B. R. 252, 186 Fed. 859 (D. C. N. Y.).

^{98.} *In re Fabacher*, 27 A. B. R. 534, 193 Fed. 556 (D. C. La.).

^{99.} *In re Allert*, 23 A. B. R. 101, 173 Fed. 691 (D. C. N. Y.).

^{1.} See form of trustees' deed, post, Appendix.

^{2.} Instance, *Snyder v. Bougher*, 16 A. B. R. 792 (Penn. Sup. Ct.), which was the case of a sale of a saloon stock and fixtures conditioned on the transfer of the license to the purchaser, where the purchaser made no effort to get the license transferred but abandoned the purchase.

^{3.} Instance, *In re Waterloo Organ Co.*, 18 A. B. R. 752, 154 Fed. 657 (C. C. A. N. Y.).

§ 2000. Jurisdiction of Suit by Third Party against Purchaser from Trustee.—No jurisdiction exists in the bankruptcy court to entertain a suit brought by a third party against the purchaser for specific performance of a contract relative to the property sold by the trustee, even though injunction against the trustee's delivery of the deed to the purchaser is part of the remedy sought and neither litigant objects to the jurisdiction.⁴

§ 2000½. Whether Injunction Available in Aid of Purchaser to Protect against Third Party.—It does not appear to be authoritatively decided whether injunction will be issued by the bankruptcy court itself after sale by the trustee in aid of the purchaser as against third parties.⁵

There is no doubt that a purchaser of the assets, including the good will and corporate name, of a bankrupt corporation will be protected in an independent suit, however, to the extent of preventing any interference with the use of such name by him, and also of preventing the old corporate name from being used by the bankrupt after its discharge in bankruptcy.⁶

§ 2000¾. Trustee of Mortgage Bondholders, Whether to Be Paid by Trustee in Bankruptcy.—In one case where a mortgage provided for a trustee for bondholders the court ordered payment direct to the bondholders, disregarding the trustee under the mortgage.⁷

4. *Henrie v. Henderson*, 16 A. B. R. 617, 145 Fed. 316 (C. C. A. W. Va., reversing *In re Henderson*, 15 A. B. R. 760).

5. Query, *In re Bluestone Bros.*, 23 A. B. R. 264, 174 Fed. 53 (D. C. W. Va.), although, on principle such ju-

risdiction should exist long enough, at any rate, to place the purchaser in possession.

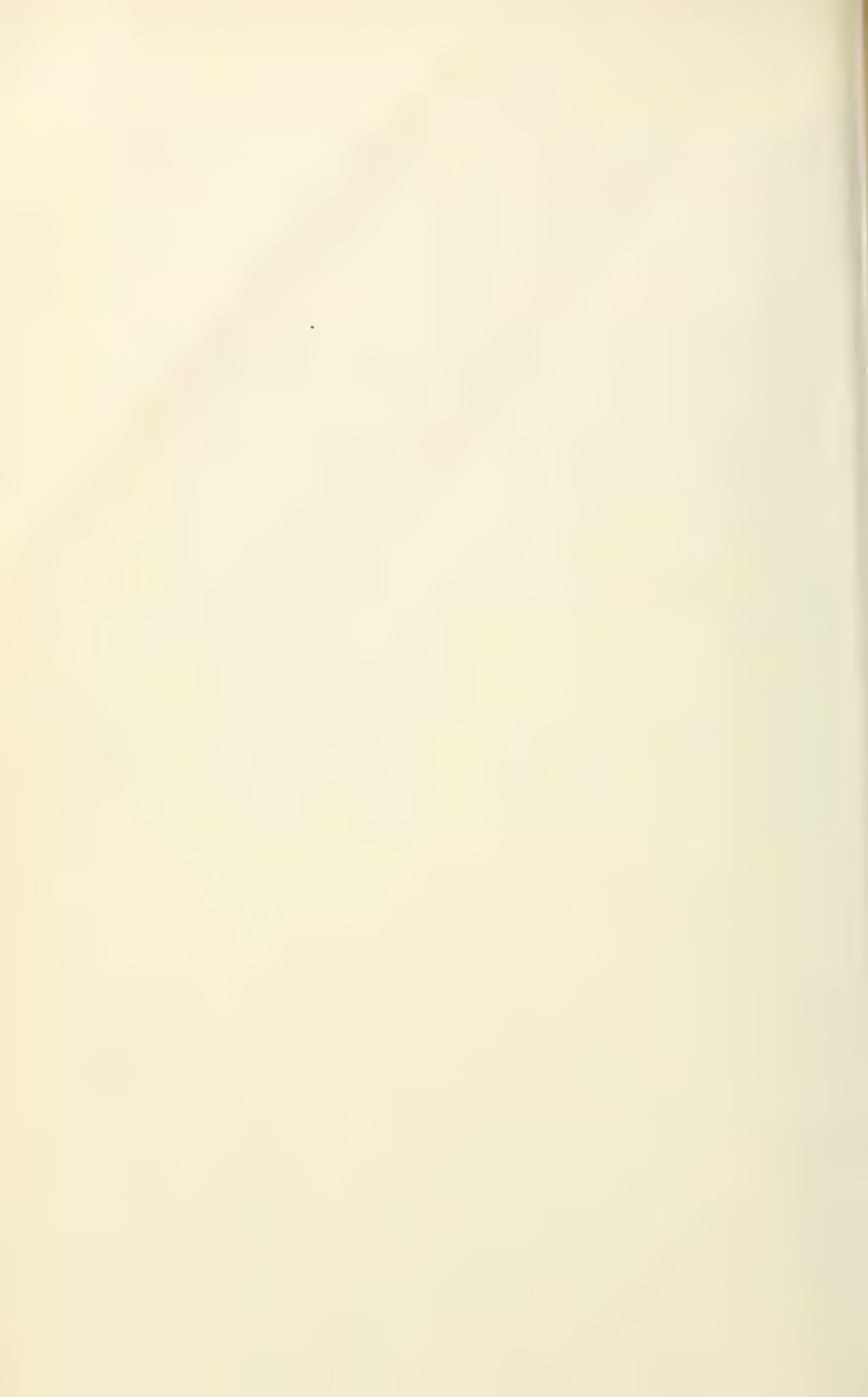
6. *Myers & Co. v. Tuttle*, 26 A. B. R. 541, 188 Fed. 532 (C. C. N. Y.).

7. *In re Chambersburg Mfg. Co.*, 26 A. B. R. 107, 190 Fed. 411 (D. C. Pa.).

PART VII.

COSTS OF ADMINISTRATION, DISTRIBUTION AND CLOSING OF ESTATES.¹

1. For costs other than those of administration, see various subjects. In the orderly arrangement of the treatise, the subjects of the collection and sale of the assets belonging to general creditors and their separation from the property of third persons and from that of the bankrupt, having been discussed, naturally is reached, next in order, the subject of costs and expenses of administration and the distribution of the remainder in dividends to creditors.



CHAPTER XL.

COSTS AND EXPENSES OF ADMINISTRATION.

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§ 2001. **Jurisdiction to Tax Costs.**—Costs may be taxed by the bankruptcy court against parties and against estates.¹

1. Bankr. Act, § 2 (18): "Tax costs, render judgments therefor against the whenever they are allowed by law, and unsuccessful party, or the successful

But, unless there be some provision of the Bankruptcy Act, expressly or impliedly authorizing the charging of expenses against the estate, only those costs may be taxed against estates, under the authority of § 2 (18) of the Bankruptcy Act, which arise in proceedings in the administration of the estate.²

§ 2002. May Be Taxed by Referee.—They may be ordered paid by the referee, as to matters before him.³

§ 2003. May Be Taxed against Successful Party, "for Cause."—They may, for cause, be taxed against the successful party.⁴

Thus, they may be taxed against the bankrupt where the creditors have unsuccessfully prosecuted appeal from an order dismissing their specifications of objections to discharge.⁵

§ 2004. No Showing of "Cause" Requisite Where Taxed against Unsuccessful Party.—It is not necessary to show cause therefor where the costs are taxed against the unsuccessful party; as, for instance, where taxed against the unsuccessful claimant to property in the custody of the bankruptcy court.⁶ But there seems to be some question whether attorney's fees of the trustee may be taxed against an unsuccessful creditor.⁷

It would seem on principle, however, that an equitable portion of the trustee's attorney's fees might under some circumstances be taxed against the unsuccessful party; indeed, there are seldom any other "costs" that can be taxed except the expenses of the trustee, among which expenses may occur attorney's fees.^{7a}

§ 2005. Stenographer's Fees Taxable as Costs.—Stenographer's fees may form part of the costs taxed against parties, as well as against the estate.⁸

party, for cause, or in part against each of the parties, and against estates, in proceedings in bankruptcy."

Compare, instance where taxed against unsuccessful claimant, *In re Shocket*, 24 A. B. R. 47, 177 Fed. 583 (D. C. R. I.), quoted at § 2111, note.

2. Compare (successful opposition by creditors to discharge, not charged against estate), *In re Kyte*, 26 A. B. R. 507, 189 Fed. 531 (D. C. Pa.). But it does not appear whether this case was decided before or after the amendment of 1910 and, in any event, the opposition was not made by the trustee, nor in his name nor was it authorized at a meeting of creditors. Quoted at § 2060½.

3. Inferentially, *In re Todd*, 6 A. B. R. 88, 109 Fed. 265 (D. C. N. Y.).

4. *In re Todd*, 6 A. B. R. 88, 109 Fed. 265 (D. C. N. Y.).

5. *In re McCrea*, 20 A. B. R. 412, 161 Fed. 246 (C. C. A. N. Y.).

6. *In re Todd*, 6 A. B. R. 88, 109 Fed. 265 (D. C. N. Y.).

7. Compare as to costs on disallowance of claim, *In re Rome*, 19 A. B. R. 820, 162 Fed. 971 (D. C. N. J.).

7a. Compare, instance of taxing expense and compensation of custodian, for preservation of property while petition pending, against unsuccessful claimant, on refusing petition for reclamation, *In re Shocket*, 24 A. B. R. 47, 177 Fed. 583 (D. C. R. I.), quoted at § 2111, note.

8. *In re Todd*, 6 A. B. R. 88, 109 Fed. 265 (D. C. N. Y.); *In re Rozinsky*, 3 A. B. R. 830, 101 Fed. 229; *In re Ellett Electric Co.*, 28 A. B. R. 453, 196 Fed. 400 (D. C. N. Y.).

§ 2006. Employment of Stenographer at Expense of Estate.—A stenographer may be employed when authorized by the court, on application of the trustee, and his compensation may be taxed against the estate, on general examinations of bankrupts and witnesses and on other proceedings, where not already included in costs adjudged in favor of a successful party against the trustee. Where taxed against the estate on general examinations of witnesses and in cases where the estate is not the unsuccessful party, the employment of the stenographer must have been authorized by the court on application of the trustee.⁹

In re Todd, 6 A. B. R. 88, 109 Fed. 265 (D. C. N. Y.): "The rule established by the late Mr. Justice Blatchford in this court, and ever since followed in regard to stenographer's fees, was that when not provided for by law, they could not be taxed in any cause, except upon a written stipulation between the attorneys. * * *

"The Bankruptcy Act of 1898 contains but a single provision authorizing the employment or payment of stenographers, namely; § 38a (5), which provides that upon the application of the trustee, the referee may authorize the employment of stenographers at the expense of the estate, at a compensation not to exceed ten cents per folio for reporting and transcribing the proceeding.

"The authority thus given to the referee, it will be noticed, can only be exercised upon the application of the trustee; the expense is in the first instance a charge against the estate, and it is not to exceed ten cents per folio.

"The above express provision and the absence of any other, prevent imposing any further charge for stenographer's fees, or the taxation of any other, except in pursuance of some stipulation made by the parties to the cause.

"In the present case there was no such stipulation; but as the stenographer's notes were rendered desirable and the application therefor was in consequence of the claimant's contesting demands, and the controversy has been adjudged against the latter, it is proper that this necessary expense to the estate should be taxed against the claimant, and it is therefore allowed to the extent of ten cents per folio, which is one-half of the bill rendered."

§ 2007. Compensation Not to Exceed Ten Cents per Folio for Taking and Transcribing.—Stenographer's fees, when taxable against the estate, are taxable at not to exceed ten cents per folio for taking and transcribing.¹⁰ Where the stenographer is not required to transcribe his notes, doubtless he may be allowed per diem compensation for taking the testimony.

It is said a different rule prevails where the examination occurs before adjudication, before a special commissioner or master in chancery.

In re Stark, 18 A. B. R. 467, 155 Fed. 694 (D. C. N. Y.): "It does not seem to the court that the provisions of § 38, subdivision 5, apply to hearings before

9. Bankr. Act, § 38 (a) (5): "Upon the application of the trustee during the examination of the bankrupts, or other proceedings, authorize the employment of stenographers at the expense of the estates at a compensation not to exceed ten cents per folio for

reporting and transcribing the proceedings."

10. Bankr. Act, § 38 (a) (5); compare ante, § 1579; also see In re Todd, 6 A. B. R. 88, 109 Fed. 265 (D. C. N. Y.); In re Ellett Elec. Co., 28 A. B. R. 453, 196 Fed. 400 (D. C. N. Y.), quoted at § 1579.

a special commissioner. The meaning of this section would seem to be that a referee in bankruptcy may make use of the services of a stenographer, when the trustee considers that the testimony should be taken, and that in such case the rate is fixed, but this rate has nothing to do with the employment of a stenographer on isolated and unusual occasions, where at the request of the creditors or of the receiver, a special hearing is had before a special commissioner. The bankruptcy law gives the court power to appoint special masters or commissioners, to hold hearings in certain special cases enumerated in section 21a. If the hearing is not a statutory hearing before a referee in bankruptcy, the provisions of § 38, as to the employment of a stenographer by the referee in bankruptcy, would not apply."

§ 2008. Costs in Contesting Claims before Election of Trustee Not Taxable against Estate.—Costs in contesting claims before the election of a trustee, incurred in the effort to control the election, are not chargeable against the estate.¹¹

§ 2009. No Costs in Personam against Parties in Summary Proceedings, Not Personally Appearing.—While it is true that in plenary actions in the bankruptcy court under favor of the Amendment of 1903, or where a party has voluntarily entered appearance, costs may be taxed by judgment in personam against the party; yet, where such is not the case and the only jurisdiction of the court arises from its possession of the res and notice upon parties claiming interests therein—such parties not appearing in response thereto—costs may not be taxed, personally, against such parties;¹² although, of course, the proportionate compensation for care, preservation and administration may be taken out of any fund thus protected.

§ 2010. No Part of General Costs of Administration to Be Taken Out of Property Not Forming Part of Assets for Administration.—No part of the general costs of administration are to be taken out of property not forming part of the assets for administration, as, for instance, in general, none out of exempt property properly scheduled and claimed;¹³ although such costs may, if otherwise proper, be taxed against the bankrupt himself in personam, although all his property be exempt.¹⁴ Nor, in general, may they be taken out of property, no title to which nor right of possession of which is in the trustee, although cases may arise in which it would be equitable to tax the expenses of preservation and a proportionate part of the compensation of the officers of the court against the successful claimant.¹⁵

11. In re Worth, 12 A. B. R. 566, 130 Fed. 927 (D. C. Iowa); In re Fletcher, 10 A. B. R. 398 (D. C. N. Y.). Inferentially, In re Mercantile Co., 2 A. B. R. 419, 95 Fed. 123 (D. C. Mo.).

12. Havens & Geddes Co. v. Pierek, 9 A. B. R. 569, 120 Fed. 244 (C. C. A. Ills.).

13. In re LeVay, 11 A. B. R. 114, 125

Fed. 990 (D. C. Pa.); In re Yeager, 25 A. B. R. 51, 182 Fed. 951 (D. C. Pa.).

14. In re Herbold, 14 A. B. R. 116 (D. C. Wash.).

15. Compare, In re Gaskill, 12 A. B. R. 251, 130 Fed. 235 (D. C. Wash.), where the court permitted the deduction of a proportionate part of the expenses of the bankruptcy proceedings

Nor, in general, may the general costs of administration be charged against lienholders, though expenses of preservation of the particular property on which they hold their liens may, in proper cases, be so charged.¹⁶

§ 2011. Policy of Act, Strictest Economy.—The policy of the act is that of strictest economy in expenses and cost of administration.¹⁷

The greatest foe to the permanency of national bankruptcy laws in this country in the past seems to have been the opportunity they have apparently afforded for extravagance in administration. The framers of the present act repeatedly manifest in the words they have used, the utmost solicitude to guard against extravagance. The chief cause of the downfall of the act of 1867 was its extravagance. Estates were swallowed up in fees and expenses until finally the very name of bankruptcy law became a synonym for licensed plundering of creditors' estates, and its administration became odious in the eyes of the people.

In *re Mercantile Co.*, 2 A. B. R. 420, 95 Fed. 123 (D. C. Mo.): "The history leading up to the adoption of the present Bankrupt Law shows that the great abuses under the preceding National Bankrupt Act, in the way of exorbitant fees, which largely consumed the assets of the bankrupt, whereby the ministerial officers grew rich upon the administration of the act, while the creditors starved, impelled Congress, in the adoption of the present Bankrupt Act, to reverse this practice, so that the Bankrupt Law should be so administered that the creditors should be the favorites of the courts, rather than the agents assisting the court in the preservation and distribution of bankrupt estates. The obvious policy of the present act, manifest throughout all its provisions respecting fees and commissions, is to reduce to the lowest minimum the expenses of administration. This is especially made manifest in the meagre fees allowed to clerks, referees, and trustees. Indeed, so inadequate is the compensation allowed to these officers that it is a matter of happy surprise to the courts that they have been able to secure the services of such competent persons to fill the places of referees and trustees. And, because of the meagre compensation allowed by the act to these officers, courts are exposed to the constant temptation to either read into the act some provision not found in its letter, or by the most liberal construction of doubtful or ambiguous terms to augment fees and commissions. This is a tendency, however, in my judgment, which it is the bounden duty of the court to resist. It is the duty of the court, from which it cannot honestly escape, in applying this statute, to give it such construction and such application as will carry out and effectuate the legislative

upon the surrendering of a trust fund.

Compare, In *re Cambridge*, 14 A. B. R. 168, 136 Fed. 983 (D. C. Mass.), where the court construed the word "disbursements" used with reference to the compensation of receivers as comprehending the value of property returned in specie to claimants.

^{16.} Compare, ante, § 1993.

^{17.} See ante, § 24, and post, § 2048. In *re Carolina Cooperage Co.*, 3 A. B. R. 154, 96 Fed. 604 (D. C. N. C.); impliedly, In *re Kyte*, 19 A. B. R. 768, 158 Fed. 121 (D. C. Pa.); In *re Marks*, 22

A. B. R. 54 (Ref. Ga.); *Dunlap Hardware Co. v. Huddleston*, 21 A. B. R. 731, 167 Fed. 433 (C. C. A. Ga.); compare, as to extravagance in allowance of appraisers' fees, note, post, § 2128.

Instance as stenographic and attorney fees. In *re Ellett Elect. Co.*, 28 A. B. R. 453, 196 Fed. 400 (D. C. N. Y.).

Bankruptcy Court Often Has to Protect Creditors against Their Own Neglect.—*Ross v. Saunders*, 5 A. B. R. 350, 105 Fed. 915 (C. C. A. Mass.).

will. Any other action by the court is but an attempt to set up and substitute the notions and inclinations of the individual judge as to which would be a reasonable compensation for services under this law for that of the Legislature, whereas, as already suggested, the court can have no policy in conflict with that of the legislative scheme."

In re Nat'l Mercantile Agency, 11 A. B. R. 451 (Ref. N. Y.): "The dominant keynote of the Bankruptcy Law as enacted by Congress, is economical administration, so that the creditors may realize the largest possible dividends from estates administered in bankruptcy. * * *

"Complaint is being made in many directions that the expenses of preliminary administration of bankrupt estates are becoming unduly large and, in many cases, entirely disproportionate to the size of the estates called upon to bear such heavy burdens."

In re Daniels, 12 A. B. R. 450, 130 Fed. 597 (D. C. Iowa): "Much criticism was made of prior Bankruptcy Acts because of the large amount of fees and expenses incurred in the administration of the bankrupt estates. It was the manifest purpose of Congress that such criticism could not rightly be made of the present law, and it fixed the compensation of referees and other officers very low. They may be inadequate in some cases, but the court is powerless to increase them. By the amendment of February 5, 1903, it is expressly provided that the court shall not allow, under any form or guise whatever, any other or further compensation for services than that expressly authorized by the act."

In re Woodard, 2 A. B. R. 339, 691, 95 Fed. 956 (D. C. N. Car.): "One of the purposes of the Act of 1898 in establishing a uniform system of bankruptcy was to avoid what was the principal cause of the repeal of the Bankruptcy Act of 1867—excessive fees and great expenses."

In re Oppenheimer, 17 A. B. R. 60 (D. C. Pa.): "Economy is strictly enjoined by the well known policy of the Bankruptcy Act in the administration of bankrupt estates."

In re Goldville Mfg. Co., 10 A. B. R. 556, 123 Fed. 579 (D. C. S. C.): "It is a part of the history of the country that one of the causes which led to the repeal of the Bankruptcy Act of 1867 was the great abuse, under the former law, whereby the estates of bankrupts were consumed by the ministerial officers of the court in enormous costs and charges; and it was the clear intent of the present Bankruptcy Law that they should be administered for the benefit of the creditors. This is manifest through all the provisions respecting fees and commissions. The compensation allowed to clerks, referees, and trustee is so meager that it is a matter of some surprise that the courts have been able to secure persons of any competency to administer the law."

In re Ketterer Mfg. Co., 19 A. B. R. 646, 156 Fed. 719 (D. C. Pa.): "Economy in the administration of estates is the policy of the present law, and is to be strictly enforced."

In re Allert, 23 A. B. R. 101, 173 Fed. 691 (D. C. N. Y.): "It should remain uppermost in the minds of litigants and attorneys practicing in the bankruptcy courts, that it is the policy of the Bankruptcy Act to administer estates with the strictest economy, to the end that fees, costs and charges should be reduced to the lowest minimum;" although in this case itself "extra" compensation was allowed the referee.

An example of the tendency towards extravagance of administration is afforded in the practice that has grown up in a few districts of appointing special masters at an increased expense to estates to perform

various parts of the duties that the referee is presumed to perform as part of the duties for which he receives his fixed compensation;¹⁸ thus, for passing upon trustee's reports and for "advising" the trustee, etc., etc.;¹⁹ for auditing receivers' accounts and determining "reasonable" compensation;²⁰ for hearing a petition for an order upon the bankrupt to surrender assets in his possession;²¹ for considering liens, which, if the bankruptcy court had any right to consider at all, would have been because such consideration was part of the referee's duties;²² to a "special commissioner" for passing on priority of expense of administration where the assets were too small to pay them in full;²³ for determining the reasonableness of a prepayment of a bankrupt's attorney's fee under § 60 (d) and § 64 (b) (3);²⁴ for taking an accounting in order to determine the proper amount for which a proof of claim should be allowed;²⁵ for determining the validity of an unfiled chattel mortgage upon property in the possession of the receiver in bankruptcy and sold by him evidently after the adjudication of bankruptcy.²⁶

The referee must not receive extra allowance, even with the consent of counsel.²⁷ He may not have extra allowance for "investigating specific liens," questions relating to which come up in the usual and ordinary course of the administration of the estate.²⁸ No per diem may be allowed to referees for sitting in the examination of the bankrupt, nor for presiding at the first meeting of creditors.²⁹

But the referee may be allowed additional compensation while acting as special master in matters expressly restricted to the judge.³⁰

Before the amendment of 1903, trustees were sometimes allowed what was termed "extra compensation" where, by consent, property covered

18. See ante, §§ 24, 522½.

19. In re Hart & Co., 18 A. B. R. 137 (D. C. Hawaii), in which "extra" compensation was allowed for "advising" the trustee in running the business of a going concern. In re Hoyt & Mitchell, 11 A. B. R. 784, 127 Fed. 968 (D. C. N. C.). Compare, upon germane subject of attorney's fees, In re Lang, 11 A. B. R. 794, 127 Fed. 755 (D. C. Tex.).

20. Apparent instance, In re Martin-Borgeson Co., 18 A. B. R. 197, 151 Fed. 780 (D. C. N. Y.).

21. In re Herskovitz, 18 A. B. R. 247, 152 Fed. 316 (D. C. N. Y.).

22. In re Hobbs, 16 A. B. R. 544, 560 (D. C. W. Va.).

Compare, In re Allert, 23 A. B. R. 101, 173 Fed. 691 (D. C. N. Y.), wherein the court allowed a referee "extra" compensation for such duty, saying it was performed outside of the referee's duties.

23. In re Gregnard Lith. Co., 19 A. B. R. 743, 155 Fed. 699 (D. C. N. Y.).

24. In re Shiebler & Co., 20 A. B. R. 777, 163 Fed. 545 (D. C. N. Y.).

25. In re Fenn, 22 A. B. R. 833, 172 Fed. 620 (D. C. Vt.).

26. In re Watts-Woodward Press Inc., 24 A. B. R. 684, 181 Fed. 71 (C. C. A. N. Y.).

27. Dressel v. North State Lumber Co., 9 A. B. R. 541, 119 Fed. 531 (D. C. N. C.).

28. In re Mammoth Pine Lumber Co., 8 A. B. R. 651, 116 Fed. 731 (D. C. Ark.).

29. In re Parker, 7 A. B. R. 132, 111 Fed. 501 (D. C. Iowa).

30. See post, § 2660. *Fellows v. Freudenthal*, 4 A. B. R. 490, 102 Fed. 731 (C. C. A. Ills.); contra, *In re Troth*, 4 A. B. R. 780, 104 Fed. 291 (D. C. Ohio). In re Grossman, 6 A. B. R. 510, 111 Fed. 507 (D. C. Mich.); *Bragassa v. St. Louis Cycle Co.*, 5 A. B. R. 700, 107 Fed. 77 (C. C. A. Tex.), quoted at § 2660. Contra, *In re Wilcox*, 19 A. B. R. 241, 156 Fed. 685 (D. C. Mich.).

with liens was sold free and clear.³¹ This is now regulated by the Amendment of 1910 to Bankr. Act, § 48. Likewise, similar extra compensation was allowed, in some instances, to the referee where an application was made outside the ordinary scope of the referee's duties.³²

§ 2012. Preliminary Deposits for Referee, Clerk and Trustee.—Consideration of the original \$15.00 for the referee's fee, \$10.00 for the clerk's fee and \$5.00 for the trustee's fee, required to be deposited by litigants at the time of instituting the bankruptcy proceedings, has been previously had.³³

These preliminary deposits do not come up for "allowance" at all. They are fixed by statute and must be paid at the beginning—unless a poverty affidavit is filed, and even in that event the prospective bankrupt, as previously noted, usually is obliged to pass a rigid examination as to his absolute inability to make the deposit before being permitted to file his bankruptcy petition without the deposit.

We are not concerned at this time with these preliminary deposits of filing fees for the referee, clerk and trustee, nor with the expenses and commissions of the referee and trustee incurred in the marshaling of liens and selling of property free from liens, which, as previously noted, are to be taxed in each instance against the particular fund itself that has been derived from the sale of the special property involved. The making of the preliminary deposit, and the paying of the expenses of the selling of the property free from liens, are supposed already to have taken place and in the orderly development of the subject we are concerned now only with the distribution of the general estate remaining in the hands of the trustee and the costs and expenses chargeable against it.

The statute, in § 64, seeks to lay down the order of priority in the distribution of bankrupt estates; but its provisions are not altogether well defined nor free from ambiguity.

DIVISION 1.

COST OF PRESERVATION OF ESTATE SUBSEQUENT TO FILING OF PETITION.

§ 2013. First "Priority"—"Actual and Necessary Cost of Preserving Estate Subsequent to Filing Petition."—The first class in the statutory order of priority is the actual and necessary cost of preserving the estate after the petition is filed.³⁴

³¹. In re Mammoth Pine Lumber Co., 8 A. B. R. 651, 116 Fed. 731 (D. C. Ark.). This would not have been "extra" compensation under the ruling in In re Mulhauser, 9 A. B. R. 80 (D. C. Ohio).

³². In re Todd, 6 A. B. R. 88, 109 Fed. 265 (D. C. N. Y.); In re Allert, 23 A. B. R. 101, 173 Fed. 691 (D. C. N. Y.).

³³. See "Deposit for Costs in Voluntary and Involuntary Cases," ante, § 285.

Clerk's Per Diem for Making References in Judge's Absence.—See ante, § 285, n.

³⁴. Bankr. Act, § 64 a (1). *Obiter*, *Sellers v. Bell*, 2 A. B. R. 543, 94 Fed. 801 (C. C. A. Ala.); In re *Heller*, 23 A. B. R. 792, 176 Fed. 656 (D. C. N. Y.).

§ 2014. What Included in Term.—Nowhere is it clearly expressed what is included within this class. Probably it does not refer to the expenses of the receiver or trustee in administering the estate, for such expense would more properly be denominated costs of administration and so come under class three.³⁵

More likely it refers rather to cases where some person, as a clerk of the bankrupt or a creditor, has been taking care of the property before any trustee or receiver has been appointed and when the estate was totally helpless and unprotected; or to cases where the bankrupt himself has been taking care of the property meanwhile;³⁶ or to cases where some officer of a state court, as a receiver, assignee or trustee, has been permitted to retain custody of the property after the filing of the petition;³⁷ or where a receiver, before adjudication in involuntary bankruptcy, has incurred or paid extraordinary obligations in preserving the values of the property in his charge, not to be termed strictly, expenses. Thus, where the receiver has paid for the renewal of a hotel license about to expire, which was the most valuable asset of the estate and which the bankrupt himself was unable to pay.³⁸ Perhaps it refers to cases where a receiver or trustee has refused to take certain steps deemed necessary for the best interests of the estate and some creditor has, on that refusal, himself gone ahead and taken the needful steps.³⁹

35. See post, § 2033; also see *In re Pickhardt*, 29 A. B. R. 524, 198 Fed. 879 (D. C. Wis.). But see *In re Gerson*, 1 A. B. R. 251 (Ref. Penna.): This case, however, on the other proposition involved is contra, in principle, to *In re Rouse. Hazard & Co.*, 1 A. B. R. 231, 91 Fed. 96 (C. C. A. Ills.), and to *In re Slomka*, 9 A. B. R. 635, 122 Fed. 630 (C. C. A. N. Y.), although in conformity with *In re Laird*, 6 A. B. R. 1, 109 Fed. 550 (C. C. A. Ohio).

36. *In re Barrow*, 3 A. B. R. 414, 98 Fed. 582 (D. C. Va.): "It appearing that the bankrupt did not omit these crops from his schedule with a fraudulent intent, he will be allowed by the trustee a reasonable compensation for the work and care bestowed on them from the date of his adjudication."

In re Hutchinson Co., 14 A. B. R. 518 (Ref. Mich.).

Obiter, Sellers v. Bell, 2 A. B. R. 543, 94 Fed. 801 (C. C. A. Ala.): "It is to be observed that in ordinary cases, whether in involuntary or in voluntary bankruptcy, the actual and necessary cost of preserving the estate subsequent to the filing of the petition and up to the qualification of the trustee will usually, and always should where he is exercising good faith, devolve upon the bankrupt himself, not at his charge and expense, but as a charge of

the first rank against the estate which he is required or has volunteered to surrender."

Instance where expenses and compensation of clerk refused as being unnecessary, *In re Nat'l Mercantile Agency*, 11 A. B. R. 451 (Ref. N. Y.). In this case it was held, that the officers and employees of a bankrupt company against which a petition in bankruptcy is filed have no right to halt the proceedings in a vain attempt to save the company and then impose the expenses of such an attempt upon the estate as a necessary cost of preserving it subsequent to the filing of the petition.

37. *In re Harson Co.*, 11 A. B. R. 514 (D. C. R. I.); *In re Pettie*, 16 A. B. R. 450, 143 Fed. 994 (D. C. Conn.).

38. *Knittel v. McGowan*, 14 A. B. R. 209 (D. C. Pa.).

39. Compare, *In re Little River Lumber Co.*, 3 A. B. R. 682, 101 Fed. 558 (D. C. Ark.): "The trustee in this case at the time this claim should have been resisted had removed from the state. Under the advice of his counsel, to the effect that he had no right to employ an attorney for the purpose of resisting fraudulent claims, he declined to employ counsel. Being away from the state, and his counsel declining to act without remuneration, the counsel

Compare, *In re Goldville Mfg. Co.*, 10 A. B. R. 557, 123 Fed. 579 (D. C. S. C.): "Certain creditors, of their own volition, have chosen to contest the mortgage, and their attorney, like any other who takes a desperate case with the expectation of a fee contingent upon the result, to be large if successful, must abide the result; or the service may be likened to that in salvage cases in the admiralty, where salvors receive no remuneration if nothing is salvaged, however arduous their efforts and however great be their expenditures of money and time. The common reward of those who fight for lost causes is the consciousness of duty done. The Supreme Court of the United States in *Hobbs v. McLean*, 117 U. S. 582, 29 L. Ed. 940, has stated the principle which governs: 'When many persons have a common interest in a trust property or fund, and one of them for the benefit of all, and at his own cost and expense, brings a suit for its preservation or administration, the court of equity in which the suit is brought will order that the plaintiff be reimbursed his outlay from the property of the trust, or by proportional contribution from those who accept the benefits of his efforts. * * * But where one brings adversary proceedings to take possession of trust property from those entitled to it, in order that he may distribute it to those who claim adversely, and fails in his purpose, it has never been held in any case brought to our notice that such person had any right to demand reimbursement of his expenses out of the trust fund, or contribution from those whose property he sought to misappropriate.'"

It may include the compensation and expenses (including attorney's fees³⁹) of a mortgagee of a chattel mortgage, executed two days before the filing of the bankruptcy petition and made for the benefit of all creditors who would assent thereto within a stated period, where the mortgagee remains in possession.⁴⁰

The bankruptcy court is itself to determine what the reasonable and necessary expense of the preservation will amount to;⁴¹ and it is not to

in this case, using the name of one of their clients, A. DeMarce, resisted the claim of O'Dwyer & Ahern and successfully defeated it, thus increasing the assets of the estate for the benefit of all the creditors to the extent of about \$1,000. The court is somewhat familiar with the services rendered in this case, and thinks the allowance made by the referee is not exorbitant. This allowance is made and goes as a part of the expenses of the administration of the estate, and is allowed under the general equity powers of the Bankrupt Court. It seems to me that, on well-recognized equitable principles an attorney who, under the circumstances of this case, intervened and successfully resisted an unjust claim, ought to be paid by the estate which was benefited by his services. The injustice of requiring the intervening creditor to pay the attorney's manifest. His distributive share of the funds preserved to the estate would not pay one-third of the attorney's fee if he were required to pay for the services.

"It is inequitable and unjust to per-

mit the other creditors to avail themselves of his services, accompanied by the necessary risk, involving costs, etc., and then share in the estate without contributing to the payment of the attorney who did the work."

Obiter, *In re Burke*, 6 A. B. R. 502 (Ref. Ohio). Also, see *In re Groves*, 2 N. B. N. & R. 466 (Ref. Ohio), where the trustee refused to make application to have a sale set aside for stifling of competition, and certain creditors then made the application themselves, the result of which was that the sale which was for \$9,000 was set aside and on resale the property brought \$22,000!!! In that case the creditors who brought the additional fund into court were held entitled to reimbursement for their expenses in so doing, as the actual and necessary cost of preserving the estate subsequent to the filing of the petition.

Compare, *In re Evans*, 8 A. B. R. 730, 116 Fed. 909 (D. C. N. Car.).

⁴⁰. *In re Hutchinson Co.*, 14 A. B. R. 518 (Ref. Mich.).

⁴¹. *In re Allen*, 3 A. B. R. 38, 96 Fed. 512 (D. C. Calif.).

be controlled by what has been actually expended, but may re-examine the actual expenditure and allow less.

The bankruptcy court should not, where a sheriff has remained in possession, after adjudication, under an attachment the lien of which has been dissolved by the adjudication, allow more for the necessary expense of the preservation than would have been the expense had the property been turned back to the bankrupt.⁴² But a different rule would probably prevail in cases where he had remained in possession after the filing of an involuntary petition and before adjudication, for in such a case it might be improper to turn the property back.⁴³

Even expenses of a receiver in the state court, preserving the property before bankruptcy, may be assessed against secured creditors, where the secured creditors' fund was benefited.⁴⁴

Petitioning creditors doubtless may also be allowed expenses for the actual and necessary cost of preserving the estate.⁴⁵

Of course attachment costs incurred before the filing of the bankruptcy petition are not included within this priority, though incurred in the preservation of the assets; but they may be allowed priority under § 64 (b) (5) if the state law assigns them priority in the administration of insolvent estates in general.⁴⁶

DIVISION 2.

REIMBURSING PETITIONING CREDITORS FOR THEIR FILING FEES AND EXPENSE OF RECOVERING PROPERTY CONCEALED OR FRAUDULENTLY TRANSFERRED BY BANKRUPT.

§ 2015. Second "Priority"—Reimbursement of Petitioning Creditors, and of Creditors Recovering Concealed Assets.—The second class in the statutory order of priority is the reimbursement of the petitioning creditors of their deposit of filing fees,⁴⁷ and the reimbursement of creditors of their reasonable expenses in recovering, for the benefit of all creditors, property concealed or transferred by the bankrupt.⁴⁸

Obiter, Sellers v. Bell, 2 A. B. R. 543, 94 Fed. 801 (C. C. A. Ala.): "The charge of the second rank is the filing fees paid by creditors in involuntary cases. The reason for restricting this to fees paid by creditors in involuntary

⁴². In re Allen, 3 A. B. R. 38, 96 Fed. 512 (D. C. Calif.).

⁴³. Compare, In re Hutchinson Co., 14 A. B. R. 518 (Ref. Mich.).

⁴⁴. In re Allison Lumber Co., 14 A. B. R. 78, 137 Fed. 643 (D. C. Ga.).

⁴⁵. In re Heller, 23 A. B. R. 792, 176 Fed. 656 (D. C. N. Y.).

⁴⁶. Compare post, § 2197. Also, see In re Amoratis, 24 A. B. R. 565, 178 Fed. 919 (C. C. A. Calif.), quoted at § 2197.

⁴⁷. Bankr. Act, § 64 (b) (2).

Gen. Ord. XXXIV: "In cases of involuntary bankruptcy, when the debtor resists an adjudication, and the court, after hearing, adjudges the debtor a bankrupt, the petitioning creditor shall recover, and be paid out of the estate, the same costs that are allowed to a party recovering in a suit in equity; and if the petition is dismissed, the debtor shall recover like costs against the petitioner."

⁴⁸. Bankr. Act, § 64 (b) (2).

cases is obvious, because where such fees are paid in voluntary cases they may be paid by the bankrupt himself out of the estate which he has to surrender, and therefore no account need be taken of them."

Of course, creditors who are petitioning creditors may be allowed, also, for their actual and necessary expenses incurred in the preservation of the estate.⁴⁹

§ 2016. Reimbursement of Creditors Recovering Concealed Assets, etc.—Where property of the bankrupt, transferred or concealed by the bankrupt either before or after the filing of the petition, has been recovered for the benefit of the estate of the bankrupt, by the efforts and at the expense of one or more creditors, such creditors are entitled to reimbursement of the reasonable expenses of such recovery.⁵⁰

In *re Felson*, 15 A. B. R. 188, 139 Fed. 275 (D. C. N. Y.): "But if the trustee should not prosecute such an inquiry and employ necessary counsel, one or more creditors, may; and if property transferred or concealed by the bankrupt is, under such circumstances, 'recovered for the benefit of the estate of the bankrupt by the efforts and at the expense of one or more creditors,' 'the reasonable expenses of such recovery' are to be allowed and paid, and such reasonable expenses are to be regarded as a debt having priority."

And, doubtless, in such cases the court of bankruptcy would probably have authority to make such reimbursement by virtue of its general equity powers, regardless of the express permission of the statute.^{50a}

The allowance for expenses in employing counsel should be made to the creditors, and not to the attorney himself, since the attorney not having an independent standing must work out his rights through the creditors.⁵¹

§ 2017. Trustee to Be Given First Opportunity.—Probably this amendment would not permit the reimbursement of creditors of their expenses incurred after the adjudication and the appointment of a trustee, in thus recovering property transferred or concealed by the bankrupt, unless they had first applied to the trustee to take the steps required and had been met by a refusal. Certainly, if there be a trustee in charge of the estate, he should be given the first opportunity to take the necessary steps, especially so when we bear in mind that, after the election of a trustee, all action

⁴⁹. In *re Heller*, 23 A. B. R. 792, 176 Fed. 656 (D. C. N. Y.).

⁵⁰. In *re Goldberg*, 16 A. B. R. 523, 144 Fed. 566 (D. C. Me.); In *re Medina Quarry Co.*, 27 A. B. R. 466, 191 Fed. 815 (C. C. A. N. Y.), reversing 25 A. B. R. 405, 182 Fed. 508. Instance (reimbursement of attachment proceedings, where sheriff preserved assets), In *re Heller*, 23 A. B. R. 792, 176 Fed. 656 (D. C. N. Y.); *obiter*, In *re Roadarmour*, 24 A. B. R. 49, 177 Fed. 379 (C. C. A. Ohio). Compare, § 2060.

^{50a}. *Obiter*, In *re Roadarmour*, 24 A. B. R. 49, 177 Fed. 379 (C. C. A. Ohio); In *re Groves*, 2 N. B. N. & R. 466 (Ref. Ohio), wherein such reimbursement, including attorneys' fees, was allowed out of the estate for setting aside a collusive sale of the assets before the Amendment of 1903 to Bankr. Act, § 64 (b) (2).

⁵¹. In *re Medina Quarry Co.*, 27 A. B. R. 466, 191 Fed. 815 (C. C. A. N. Y.), reversing 25 A. B. R. 405, 182 Fed. 508.

in behalf of creditors must be taken in his name.⁵²

Impliedly, *In re Felson*, 15 A. B. R. 189, 139 Fed. 275 (D. C. N. Y.): "It will not do, even under the provisions of subdivision 'b' of § 64, as amended, to permit creditors generally to come with their attorneys to the aid of the trustee seeking to recover property belonging to the estate in bankruptcy of the bankrupt, and concealed by him in violation of § 29 of the Act * * * and have an allowance for their expenses or attorney's charges out of the estate. The amendment gives no such license as this, and clearly such a course was not permissible prior to the amendment. * * *

"As already stated, allowances to general creditors, one or more, who employ and pay counsel and incur and pay other expenses in doing things to benefit and increase the estate, and which have that effect, cannot be made unless the trustee has not been appointed at the time it is done, or, having been appointed, he has neglected or refused to act in the matter. Even in such case, unless there be an emergency demanding immediate action, the order and direction of the court should be first sought."

§ 2018. Disallowance of Unjust Claims before Election of Trustee.—This amendment probably would not fairly apply to a resistance of the allowance of an unjust claim to share in dividends or to vote, even where the trustee has refused to act, unless in some way such claim be connected with a "recovery" of property "transferred" or "concealed" by the bankrupt.⁵³ It is somewhat sophistical to say that the defeating of an unjust claim is a "recovery" of property because of its effect in increasing the dividends of other creditors—much less that it is a recovery of property "transferred" or "concealed" by the bankrupt.^{53a}

In re Medina Quarry Co., 27 A. B. R. 466, 191 Fed. 815 (C. C. A. N. Y., reversing S. C., 25 A. B. R. 405, 182 Fed. 815, D. C. N. Y.): "Evidently the district judge, in making allowances to these attorneys, took into consideration services which were helpful in rejecting claims, setting aside claimed priorities, and in securing the appointment of a proper trustee. But it cannot be said that these were services which resulted in the recovery of any property, within the meaning of the statute, or which created any fund which would justify allowances under general equity powers."

In re Worth, 12 A. B. R. 572, 130 Fed. 927 (D. C. Iowa): "In the matter of costs, the contest was wholly between creditors of the estate, and, while it is claimed in behalf of the objecting creditors that they were waging it in the interest of the estate, it clearly appears that it was in fact waged for the purpose of controlling the election of the trustee. No reason appears why the estate should bear the cost of such a contest."

Nevertheless, a creditor opposing the allowance of an unjust claim might be allowed to use the trustee's name if the trustee refuses to act, and thus,

⁵². *In re Medina Quarry Co.*, 25 A. B. R. 405, 182 Fed. 508 (D. C. N. Y.), reversed on other points in S. C., 27 A. B. R. 466, 191 Fed. 815 (C. C. A. N. Y.).
Injunction until bankruptcy petition can be filed, before amendment of 1903: *Vietor v. Lewis*, 1 A. B. R. 667 (N. Y. Sup. Ct. App.).

⁵³. To same effect, *In re Felson*, 15

A. B. R. 185, 139 Fed. 275 (D. C. N. Y.); compare, *In re Groves*, 2 N. B. N. & R. 466 (Ref. Ohio). Contra, *In re Little River Lumber Co.*, 3 A. B. R. 682, 101 Fed. 558 (D. C. Ark.).

^{53a}. See post, §§ 2057, 2071; also see, inferentially, *In re Mercantile Co.*, 2 A. B. R. 419, 95 Fed. 123 (D. C. Mo.), quoted at § 2057.

if successful, might have his attorneys' fees charged against the estate as part of the trustee's expenses.⁵⁴

Even before the amendment of 1903 allowing reimbursement to creditors, in certain instances creditors were allowed their expenses in recovering assets for the benefit of the estate where there was no receiver, marshal nor trustee yet in charge, or where such officers had refused to act, the allowance being based upon the principle that such expenses were an equitable lien on the fund.⁵⁵

Even before the amendment of 1903, and in cases where creditors had been simply acting for themselves, they have been held entitled to have their expenses declared a lien upon the fund thus seized by them.⁵⁶

In *re Lesser Bros.*, 5 A. B. R. 320, 180 Fed. 201 (C. C. A. N. Y.): "In this case, the appellants have, by a litigation which lasted about three and one-fourth years and went through two appellate courts, obtained, without aid from any other creditor, a fund of \$27,000 for the benefit of all the creditors from fraudulent insolvents, who, at the last moment went into bankruptcy, apparently to prevent the appellants from obtaining a substantial benefit from the protracted and expensive litigation. The outcome, so far as the appellants are concerned, seems inequitable. We think that the order should be so modified as to permit them to become parties in the proceedings by the trustee in bankruptcy in the State court, and present to that court such consideration and facts as may bear upon an application for an allowance to them from the fund, in the nature of a reasonable compensation for their costs, expenses and disbursements in the litigation which resulted in the defeat of the fraudulent attempts of the bankrupts, in wresting the fund from the hands of receivers applied for in fraud of creditors and in its preservation for their actual benefit." This case was reversed by the Supreme Court sub nom. *Metcalf v. Barker*, 9 A. B. R. 36, 187 U. S. 165, but upon the ground that the lien was not obtained within the four months, so its authority upon the point in question is not affected.

Also, undoubtedly, where under § 67 (f) a lien obtained by legal proceedings, dissolved by the adjudication, is preserved for the benefit of all creditors, the costs of court would also be entitled to payment in full as part of the lien upon the fund;⁵⁷ also, perhaps, under § 64 (b) (5), where such costs have been granted priority under state law in cases of subsequent equitable sequestrations of property.⁵⁸

The clause added by the amendment of 1903 to § 64 (b) (2) undoubtedly suggests a proper course to be pursued by creditors after the filing of an involuntary petition in bankruptcy, and before adjudication, where no receiver is appointed and necessity exists for steps to be taken to recover

54. Compare, *In re Little River Lumber Co.*, 3 A. B. R. 682, 101 Fed. 558 (D. C. Ark.).

55. *In re Groves*, 2 N. B. N. & R. 466 (Ref. Ohio).

56. Compare, evident practice, *In re Ogles*, 2 A. B. R. 514 (Ref. Tenn.). But compare, contra, inferentially, *In re Smith*, 5 A. B. R. 559, 108 Fed. 39 (D. C. N. Car.). Also, compare, contra,

In re Silverman, 3 A. B. R. 227, 97 Fed. 325 (D. C. N. Y.). Compare (though occurring after the Amendment of 1903), *In re Heller*, 23 A. B. R. 792, 176 Fed. 656 (D. C. N. Y.).

57. *Receivers v. Staake*, 13 A. B. R. 281, 133 Fed. 717 (C. C. A. Va.); *In re Lesser Bros.*, 5 A. B. R. 320, 108 Fed. 201 (C. C. A. N. Y.).

58. Post, § 2197.

property transferred or concealed either before or after the filing of the petition. In such cases no provisional seizure of the property could be had by the marshal or a receiver, under § 69 and § 3 (e), for such seizure is not permissible except as to property in the hands of the bankrupt or his agent and is forbidden where the property is in the hands of an adverse claimant such as an alleged fraudulent transferee; it being further questionable whether a receiver has the power to institute suits for such recovery prior to adjudication. In such a situation, if creditors are to be protected before adjudication, it is proper for them to institute proceedings in the state courts to set aside the alleged fraudulent transfer and to recover the property, whereupon, if subsequently the debtor be adjudged bankrupt, their costs and expenses would be entitled to priority, for it would be through their "efforts" that the property would finally have been recovered for the benefit of all.

But it has been held proper, probably under this section, to reimburse attaching creditors for their attorney's fees and other expenses incurred in levying attachments on the debtor's property within four months of bankruptcy for their own benefit, the lien of the attachments being void as to the creditors in bankruptcy, but being preserved for the benefit of the estate, since thereby an unfiled or unrecorded instrument was rendered void.⁵⁹ But there would seem to be no more reason for reimbursing such levying creditors than for reimbursing any other creditors who had sought to gain an advantage by levying but had failed.

DIVISION 3.

"COSTS OF ADMINISTRATION;" REFEREE'S, TRUSTEE'S AND RECEIVER'S EXPENSES AND COMPENSATION; ATTORNEYS' FEES; APPRAISERS' AND WITNESS' FEES, ETC.

§ 2019. Third Priority—"Costs of Administration."—The classification of priorities given in § 64 of the act is somewhat misleading, since that section perhaps would imply that the costs of the preservation of the estate subsequent to the filing of the petition and the filing fees of the petitioning creditors already provided for in classes one and two are not also part of the "costs of administration."⁶⁰

In this third class undoubtedly come the receiver's and trustee's expenses, including attorneys' fees; also, of course, the allowance of compensation to appraisers; the attorney's fees for the bankrupt and for the petitioning creditors; and the fees and mileage of witnesses and of the bankrupt. Also

^{59.} *Receivers v. Staake*, 13 A. B. R. 281, 133 Fed. 717 (C. C. A. Va., affirmed sub nom. *First Nat'l Bk. v. Staake*, 15 A. B. R. 639, 202 U. S. 141).

Compare (though lien of attachment not preserved for benefit of estate), In

re *Heller*, 23 A. B. R. 792, 176 Fed. 656 (D. C. N. Y.).

^{60.} **Ambiguity of Term "Costs of Administration."**—The term "costs of administration" is ambiguous. Compare, In re *Kross*, 3 A. B. R. 189, 96 Fed. 819 (D. C. N. Y.).

in this class undoubtedly comes the referee's reimbursement of his expenses in sending and publishing notices and for office rent, clerk hire, etc.

In fact this third class comprehends almost all the costs and expenses, and there is nothing prior to it except the actual and necessary cost of preserving the estate, and the filing fees of petitioning creditors, and also the reimbursement of creditors who have brought funds into the estate, whose reimbursement of course always is more than counterbalanced by the fund recovered, so the nominal precedence is never likely to occasion conflict, the rights of such creditors being in the nature of a lien upon the fund brought into the court, rather than a claim for priority of payment.

§ 2020. Equity Rules to Govern Order of Precedence in Class Three.—As to the priority of the different items of costs and expenses of this class three among themselves, no rule is laid down by the statute itself, so the ordinary equity rules are to be appealed to for guidance.⁶¹

§ 2021. Indemnifying Court Officers and Advancing Moneys for Expenses.—The referee, clerk and marshal are authorized to require indemnity for expenses from the person in whose behalf the duty is to be performed.⁶²

§ 2022. Reimbursement of Expenses Advanced.—The person so indemnifying is entitled to reimbursement of the amounts so advanced, as part of the cost of administration.⁶³

Even as to discharge expenses, the bankrupt is entitled to reimbursement for amounts advanced by him to pay the expense of issuing, mailing and publishing notices to creditors of his application for discharge.⁶⁴

§ 2023. No Reimbursement of Original Deposit Except to Petitioning Creditors.—Such right to reimbursement, however, does not apply to the thirty dollars preliminary deposit of fees for the referee, clerk and trustee, except to those deposited by petitioning creditors, but applies only to moneys advanced to pay expenses. Such preliminary deposits, where they are made by the bankrupt himself, would belong to the estate as part of the bankrupt's property.

In *re Matthews*, 3 A. B. R. 265, 97 Fed. 772 (D. C. Iowa): "The provisions of General Order No. 10 do not apply to the deposit of \$25, which the clerk, under § 51 of the Bankrupt Act, [before the Amendment of 1903 increased it to \$30.] is required to collect from the bankrupt when he files his petition. The money thus collected by the clerk is intended to cover the statutory fees to be paid to the clerk, referee, and trustee as compensation for their services; and being paid to the clerk when the petition is filed, the amount of the estate passing to the trustee is lessened by that sum, and, if this amount should be

61. In *re Burke*, 6 A. B. R. 502 (Ref. Ohio). See post, § 2027.

62. Gen. Order No. X.

63. Gen. Order No. X. In *re Hatcher*, 16 A. B. R. 722, 145 Fed.

658 (D. C. Tex.); In *re [Ralph] Carpenter*, 25 A. B. R. 161 (Ref. N. Y.).

64. In *re Hatcher*, 16 A. B. R. 722, 145 Fed. 658 (D. C. Tex.).

now returned to the bankrupt, he would be receiving part of his estate as it belonged to him before he filed his petition, which estate by the adjudication became in fact the property of the creditors. The provisions of General Order No. 10 are intended to cover money which the bankrupt or some third party may be called upon to furnish after the initiation of the proceedings in order to meet expenses incurred by the officer for the purposes specially recited in the order, which purposes do not include the money deposited with the clerk to meet the fees (not expenses) of the clerk, referee and trustee. Money thus advanced, if the bankrupt has met the requirements of the law with respect to turning over his estate to his creditors, is deemed to have been obtained from sources other than the estate belonging to the creditors, and therefore provision is made for its repayment out of the estate. The purpose of the order is to protect the officers from personal loss in the performance of their duties under the Bankrupt Act, but it is not the intent of the order that the bankrupt shall be repaid the money which presumably he took out of his estate to pay the fees of officers before he filed his petition in bankruptcy."

§ 2024. Nor of Attorney's Fees Paid by Bankrupt in Advance.

—A bankrupt, of course, is not entitled to reimbursement of attorney's fees paid by him in advance of filing the petition.

In re Matthews, 3 A. B. R. 265, 97 Fed. 772 (D. C. Iowa): "These services have been paid for, however, and the payment was made out of the estate of the bankrupt; so that, in effect, the creditors have already made good the amount. If the bankrupt had not paid this sum to his attorney, it would have formed part of his estate, which he would have been in duty bound to transfer to his trustee."

§ 2025. No Reimbursement of Bankrupt for Care of Exempt Property.—A bankrupt is not entitled to reimbursement of his expenses in taking care of exempt property pending its being set off to him.⁶⁵ On the contrary the rent and storage charges for the care of exempt property, pending its being set apart to the bankrupt, are properly chargeable against the bankrupt.⁶⁶

§ 2026. Reimbursement to Follow Order of Priority of Expenses Themselves.—In reimbursing the bankrupt or a creditor, under rule ten of the Supreme Court's General Orders, for money advanced to defray the expenses of the referee, marshal or clerk, such reimbursement has the same priority that the expenses themselves would have had, the one making the advancement being subrogated to the rights of the officer whose expenses are advanced.⁶⁷

§ 2027. Probable Order of Priority.—Undoubtedly, the expenses of the referee, receiver and trustee would in equity have precedence over all other costs of administration; ^{67a} and probably the order of priority in this

65. In re Groves, 6 A. B. R. 728 (Ref. Ohio, affirmed D. C.).

66. In re Grimes, 2 A. B. R. 730, 96 Fed. 529 (D. C. N. Car.).

67. In re Burke, 6 A. B. R. 502 (Ref. Ohio.).

67a. But compare, In re Gregnard

Lith. Co., 19 A. B. R. 743, 155 Fed. 699 (D. C. N. Y.), in which case occurs the remarkable item of "special commissioner's" fees for passing upon the priority of expenses of administration where the estate is not sufficient to pay them in full! See ante, §§ 24, 2011.

class three—Costs of Administration—would be somewhat as follows:

First, referee's expenses for mailing and publishing notices and for office rent and clerk hire, and for traveling, etc.

Second, receiver's and trustee's expenses, including attorneys' fees and rent, insurance, watchman, stenographers' fees,⁶⁸ and other expenses, as various as the different cases themselves are variant.

Third, bankrupt's attorney's fees and the attorney's fees and other expenses of the petitioning creditors.

Fourth, appraisers' fees.

Fifth, witness' fees and mileage.

Sixth, commissions and compensation, other than the deposit of filing fees already considered, for the referee, receiver and trustee.

SUBDIVISION "A."

REFEREE'S EXPENSES.

§ 2028. **Referee's Expenses.**—The referee is entitled to reimbursement of his expenses, and may require indemnity therefor.⁶⁹

He is entitled to require indemnity for his expenses, by the Supreme Court's General Order No. X. Were he not entitled to indemnity, it would yet doubtless be the law, from the necessities of the case, that his expenses would come first, even though not mentioned first in the statutory order of priority; for his expenses are the expenses of the maintenance of the court itself, and the expenses of the government in thus protecting the rights of parties in a particular fund or property is to be considered a first lien upon the fund or property, ahead of all liens thereon created by the parties themselves, as well as ahead of the lien of the government thereon for taxes for general purposes.

§ 2029. **"Expenses" Not Covered by Statutory Compensation of Referee, Receiver and Trustee.**—The limitation of the referee's, receiver's and trustee's compensation so carefully guarded in § 72 of the act in the following words: "That neither the referee, receiver, marshal, nor trustee shall in any form or guise receive, nor shall the court allow him, any other or further compensation for his services than that expressly authorized and prescribed in this act," does not prevent the referee, receiver nor trustee from being reimbursed for expenses.⁷⁰

68. In re Todd, 6 A. B. R. 88, 109 Fed. 265 (D. C. N. Y.). Compare (not allowed for the benefit of general creditors at the sacrifice of priority creditors), In re Rozinsky, 3 A. B. R. 830, 101 Fed. 229 (D. C. N. Y.).

69. Bankr. Act, § 62 (a). Gen. Order XXXV; Gen. Order X.

70. Bankr. Act, § 62 (a): "The actual and necessary expenses incurred by officers in the administration of es-

tates shall, except where other provisions are made for their payment, be reported in detail under oath, and examined and approved or disapproved by the court. If approved they shall be paid or allowed out of the estates in which they were incurred."

Rule XXXV of the Supreme Court's General Orders: "2. The compensation of referees, prescribed by the act, shall be in full compensation for all services

§ 2030. What Are Proper Expenses of Referee.—The referee's expenses proper for reimbursement as part of the costs of administration are, in general, those for mailing notices to creditors and publishing notices in the newspaper of the bankrupt's adjudication and of his application for discharge; for necessary stationery, printing, office rent and supplies and clerk hire; and traveling expenses and other similar expenses that are necessary.

Thus, the referee's expenses for the publication of notice of the application for discharge, for stationery, etc., are properly chargeable against the estate.⁷¹ And the referee may be allowed, by special order of the judge, his traveling and hotel expenses and amounts paid stenographers, when a detailed account thereof, verified by his oath that they were necessarily and actually incurred, is returned to the bankruptcy court with the proper vouchers, when procurable, as provided by the general orders in bankruptcy.⁷²

But he is not to be given an extra allowance as compensation for his services merely because they were performed away from home:⁷³ he is limited to his statutory compensation. Nor should he be allowed the expenses of a clerk away from home unless the necessity therefor is shown by special circumstances.⁷⁴

The referee may be allowed clerk hire, where reasonably necessary in the discharge of his duties.⁷⁵

In *re Tebo*, 4 A. B. R. 235, 101 Fed. 419 (D. C. W. Va.): "In regard to the allowance of clerk hire, the court is of the opinion that no referee can, without

performed by them under the act, or under these general orders; but shall not include expenses necessarily incurred by them in publishing or mailing notices, in traveling, or in perpetuating testimony, or other expenses necessarily incurred in the performance of their duties under the act and allowed by special order of the judge.

"3. The compensation allowed to trustee under this Act, etc., etc."

Rule X of the Supreme Court's General Orders: "Before incurring any expense in publishing or mailing notices, or in traveling, or in procuring attendance of witnesses, or in perpetuating testimony, the clerk, marshal or referee may require, from the bankrupt or other person in whose behalf the duty is to be performed, indemnity for such expense. Money advanced for this purpose by the bankrupt or other person shall be repaid him out of the estate as part of the cost of administering the same."

Impliedly, In *re Daniels*, 12 A. B. R. 446, 130 Fed. 597 (D. C. Iowa); In *re Elk Valley Coal Mining Co.*, 32 A. B. R. 197, 210 Fed. 386 (D. C. Ky.).

71. In *re Dixon*, 8 A. B. R. 145, 114 Fed. 675 (D. C. Calif.).

72. In *re Daniels*, 12 A. B. R. 446, 130 Fed. 597 (D. C. Iowa); In *re Elk Valley Coal Mining Co.*, 32 A. B. R. 197, 210 Fed. 386 (D. C. Ky.).

73. In *re Elk Valley Coal Mining Co.*, 32 A. B. R. 197, 210 Fed. 386 (D. C. Ky.).

74. In *re Elk Valley Coal Mining Co.*, 32 A. B. R. 197, 210 Fed. 386 (D. C. Ky.).

75. *Contra*, In *re Carolina Cooperage Co.*, 3 A. B. R. 154, 96 Fed. 604 (D. C. N. Car.): This case lays down too broad a rule. Instead of limiting the reimbursement for clerical assistance to cases where it is necessary, the court broadly prohibits it altogether. Evidently the court had not in mind the cases of estates where hundreds of notices are to be sent and where hundreds of claims come pouring in at the first meeting, etc. In such cases to compel the referee to do all the work himself would be an absurdity. The opinion does not lay down safe law.

the aid of the clerk or such other officer as he may require, discharge his public duties. This is a matter largely within the discretion of the referee, which discretion, if abused, would justify the court in removing him. While Bankrupt Act, § 64b, par. 3, does not mention clerk hire as being embraced in the costs of administration, yet the paragraph does not forbid it, and this court is of the opinion that it is a necessary incident to the referee in the due administration of his office, as he is, in fact, the judge of the bankrupt court."

§ 2031. No Reimbursement Where Expenses Not Required by Act or Rules.—The referee is not entitled to reimbursement from the estate of his expenses incurred in mailing notices to creditors that are not required by law to be mailed. Thus, he is not entitled to reimbursement for mailing notices to all creditors of the re-examination of a creditor's claim, although properly entitled to reimbursement for the sending of the notice to the creditor himself. Nor is he entitled to reimbursement for notices of protests against the confirmation of a sale;⁷⁶ nor for making copies of the petition for discharge;⁷⁷ nor for stenographer's fees, unless by stipulation of parties, or where employed upon application of the trustee.⁷⁸

§ 2032. Method of Apportioning Expenses.—In order to meet the difficulty of estimating for each case the proportion of expenses for such case, the district courts have laid down certain rules which roughly apportion these expenses. Thus, in several districts, ten cents for each notice sent to creditors is the rule, this charge being estimated to about cover the actual expenses of the referee for office rent, clerk hire, publishing notices in the newspapers, etc., etc.

This ten cents per notice is not chargeable as a fee, but as a means of covering estimated expenses.⁷⁹

SUBDIVISION "B."

RECEIVER'S AND TRUSTEE'S EXPENSES.

§ 2033. Expenses of Receivers and Trustees.—Of course the expenses of receivers and trustees are bound to be various.⁸⁰

They are as varied as are the natures of the different businesses that happen to get into bankruptcy. Thus, there is likely to be rent,⁸¹ expenses of conducting the business, insurance,⁸² watchman's hire, clerk hire, appraisers' fees,⁸³ expense of litigation; attorneys' fees; etc.

^{76.} In re Mammoth Pine Lumber Co., 8 A. B. R. 651, 109 Fed. 308 (D. C. Ark.).

^{77.} In re Dixon, 8 A. B. R. 145, 114 Fed. 675 (D. C. Calif.).

^{78.} In re Mammoth Pine Lumber Co., 8 A. B. R. 651, 109 Fed. 308 (D. C. Ark.); In re Todd, 6 A. B. R. 88 (D. C. N. Y.). But see In re Daniels, 12 A. B. R. 446, 130 Fed. 597 (D. C. Iowa).

^{79.} Analogously, In re Hardware & Furn. Co., 14 A. B. R. 186, 134 Fed. 997 (D. C. N. C.).

^{80.} **Withholding Expenses on Removal of Trustee.**—Under what circumstances the allowance of expenses has been withheld on removal of the trustee, see In re Leverton, 19 A. B. R. 434, 155 Fed. 925 (D. C. Pa.); also, see ante, § 947½.

^{81.} In re Hersey, 22 A. B. R. 860, 171 Fed. 998 (D. C. Iowa).

^{82.} In re Kyte, 19 A. B. R. 768, 158 Fed. 121 (D. C. Pa.).

^{83.} See ante, § 1930½, note.

It has been said that it primarily rests upon the receiver or trustee to perform the duties personally and that only in instances where he cannot reasonably do so may he get assistance from others.⁸⁴

In *re Pickhardt*, 29 A. B. R. 524, 198 Fed. 879 (D. C. Wis.): "A receiver or trustee in bankruptcy, whatever other duties may be cast upon him, is certainly the legal and actual custodian of the property which is the subject of the proceeding; and, under the rule of this court (bankruptcy rule No. 3), a receiver, unless otherwise ordered, can 'act only as custodian to care for the property (and have the same insured) for delivery to the trustee.' It is rightly presumed that the duty to so act, as every other duty, must, in the first instance, be performed by the receiver or the trustee personally, as an incident to or burden of the office, and in consideration of whatever compensation may be allowed. The right to assistance, at the cost of the property in custody, in addition to such compensation, must arise out of circumstances or conditions disclosing a burden beyond the reasonable possibility of performance by the single individual charged therewith. Such situations are found when the property is of great bulk, situated in different localities, or where, in its care and preservation, service of a special or unusual character is required."

A receiver whose negligence causes unnecessary expense to the estate may not only be denied his commissions, but he may also be charged with such expense.⁸⁵

In *re Tisch*, 29 A. B. R. 339, 202 Fed. 1018 (D. C. N. Y.): "I concur with the referee in his finding that the receiver's attorneys were guilty of gross neglect of duty. In my opinion the receiver was guilty of similar neglect, and should be allowed no commissions. I think also that the receiver should be charged with the custodian's fees. There was no need of custodians. The bankrupt's assets consisted of a small lot of jewelry worth about \$1,200, a large safe and some show cases. The assets might have been put in the safe and the safe locked; or if, for any reason, it was deemed objectionable to leave them in the safe, they could have been stored at slight expense. Apparently the custodian's services consisted in watching the safe and the show cases, but there could not have been much danger of burglars stealing them. If the custodians have rendered the service they should be paid by the trustee, but the amounts paid should be charged to the receiver. Some receivers seem to suppose that custodians are to be employed in every case. They are not required in most cases. If a receiver takes the same care of the assets that a prudent man takes of his own property, that is ordinarily enough. I have felt considerable doubt whether the receiver should not be charged with a part of the rent. Receivers should allow bankrupts only a reasonable time in which to try to effect a settlement or a composition. Usually a month is enough."

§ 2034. Rent for Use and Occupation.—Receivers and trustees in bankruptcy are entitled to occupy the premises occupied by the bankrupt at the time of bankruptcy for a reasonable time, sufficient not only for the safe and proper removal of the assets therefrom, but also for the prevention of loss of value or deterioration where sale on the premises is de-

⁸⁴. In *re Pickhardt*, 29 A. B. R. 524, 198 Fed. 879 (D. C. Wis.).

⁸⁵. See post, § 2113.

sirable.⁸⁶ And this is so even though the lease be broken and forfeited, and right of re-entry has become fixed at law, provided adequate compensation for use and occupation can be made.

In *re Chambers, Calder & Co.*, 3 A. B. R. 537, 98 Fed. 865 (D. C. R. I.): "Execution in ejectment would, in the present case, interfere with the possession of this court, and on that ground alone might be enjoined. It is furthermore apparent that it would most seriously embarrass this court, in the administration of the bankrupt's estate, and result in unnecessary loss to the creditors. There is trustworthy and undisputed evidence that the stock of goods on the leased premises is such that their proper packing and safe removal from the premises cannot be accomplished in much, if any, less than four weeks. A tenant, even though the conditions of his lease is broken by nonpayment, has such legal right of ingress and egress as is necessary for the removal of personal property. There could be little practical value to the landlord in the possession of the premises during this time, and there is no suggestion of any facts indicating that pecuniary compensation will not be entirely adequate for a reasonable delay in the surrender of the premises."

But the landlord is entitled to pay for the use and occupation of the premises,⁸⁷ such being by way of an expense of the administration and not by way of a "priority."⁸⁸

§ 2035. **Whether Computed at Lease Rate.**—Receivers and trustees occupying premises held by the bankrupt under lease are, in general, bound to pay for the use and occupation at the rate prescribed by the lease for rent;⁸⁹ until adjudication in bankruptcy, at any rate;⁹⁰ although it is

^{86.} *Bray v. Cobb*, 3 A. B. R. 788, 100 Fed. 270 (reversed, on other grounds, in *Cobb v. Overman*, 6 A. B. R. 324, 109 Fed. 65 (C. C. A. N. Car.). See ante, § 984.

^{87.} In *re Grignard Lith. Co.*, 19 A. B. R. 101, 158 Fed. 557 (D. C. N. Y.); In *re Hersey*, 22 A. B. R. 860, 171 Fed. 998 (D. C. Iowa).

Restraining Action in Personam by Landlord against Trustee.—A landlord has been restrained from prosecuting an independent suit in personam for trespass against the trustee where, as the bankruptcy court found, he was endeavoring in this manner to recover rent for use and occupation, having delayed presenting his bill therefor as a part of the expenses of administration until almost all the funds of the estate had been disbursed. In *re Empire Construction Co.*, 19 A. B. R. 704, 157 Fed. 495 (D. C. N. Y.). This case was reversed on appeal (S. C., 166 Fed. 1019, C. C. A. N. Y.) in a memorandum opinion which was based on the doctrine that it was an impropriety on the part of the bankruptcy court to say that the action sounded in contract when the state court held that it was founded in trespass. It might be

added, moreover, that this was one of the expenses of the receivership in any event, and the trustee properly might have been held personally liable therefor in an action on contract, under the doctrine of § 1780½, "Debts Contracted as Receiver."

^{88.} In *re Hersey*, 22 A. B. R. 860, 171 Fed. 998 (D. C. Iowa).

^{89.} In *re Gerson*, 2 A. B. R. 170 (D. C. Penna.). In *re Kelly Dry Goods Co.*, 4 A. B. R. 530, 102 Fed. 747 (D. C. Wis.). Instance, *Wilson v. Penna. Trust Co.*, 8 A. B. R. 169, 114 Fed. 742 (C. C. A. Penna.); instance, In *re Winfield Mfg. Co.*, 15 A. B. R. 257 (D. C. Pa.).

But see, impliedly, contra, and to the effect that reasonable compensation for use and occupation is the sole measure, In *re Chambers, Calder & Co.*, 3 A. B. R. 537, 98 Fed. 865 (D. C. R. I.).

In *re Cronson*, 1 N. B. N. 474 (Ref. Pa.): In this case the stipulated rent was held also to be the reasonable rent.

In *re Gerson*, 1 N. B. N. 315 (Ref. Pa.). See ante § 985.

^{90.} In *re Hinckel Brew. Co.*, 10 A. B. R. 484, 123 Fed. 942 (D. C. N. Y.).

not by virtue of being bound by the terms of the lease, but rather because its terms must be taken to be the best measure of the value of the use and occupation. Nevertheless, the lease is not, in all cases, to be considered as fixing the actual value.⁹¹

In re Yodleman-Walsh Foundry Co., 21 A. B. R. 509, 166 Fed. 381 (D. C. N. Y.): "This court has held in a number of instances that if the receiver is actually in possession, for the purpose of preserving the estate, during a certain number of days, he should pay, as part of the expenses of maintaining the estate, the pro rata rent, at a reasonable value, for that time, and in the same way this court has held in a number of instances that the receiver is entitled to the benefit of being compelled to pay only a reasonable value for the property, if the rental value happens to be greater because of some contract liability which will result in a claim against the estate in the hands of the trustee, or against the bankrupt himself, if he should subsequently continue with the lease."

It is doubtful, also, whether the landlord's loss of a prospective tenant by reason of the occupancy can be taken into account in arriving at a quantum valebat.⁹²

§ 2035¹/₂. Trustee's or Receiver's Use of Property Sold on Conditional Sale.—A conditional vendor must take some positive step, probably by way of order of the court, if he wishes to charge the receiver or trustee for the use of the property conditionally sold, pending litigation over its title.

In re Daterson Pub. Co., 26 A. B. R. 582, 188 Fed. 64 (C. C. A. Pa.): "The trustee never elected to take these articles as belonging to the estate, nor were the vendors willing he should. On the contrary, the vendors claimed, retained, and were decreed, to have the title of the property in themselves. They contend, however, that while the question of their title was being determined by the court, the machines remained in the possession of the trustee, and for such period the estate should pay at the rental rate fixed by the contract. But this is a non sequitur. If during such period the trustee used the machines, he could have been prevented from doing so on complaint to the court; for its general order permitting him to continue business for a limited period did not authorize him in doing so to use other peoples property without their consent. Or, if he used it without formal permission of the owner, the court would no doubt, on a proper showing have directed him to pay a proper sum for such use and occupation. But, whatever might have been the rights of the petitioners, no such relief was sought, nor have we before us proof of facts which would enable us to take any such action."

§ 2036. Expense of Conducting Business.—When the receiver or trustee has been authorized to conduct the business, the expense of conducting it is a proper charge against the estate.⁹³ And this is so even

91. See ante, §§ 667, 985; also, see In re Adams Cloak, etc., House, 28 A. B. R. 923, 199 Fed. 337 (D. C. Mass.).

Trustee is not liable for use and occupation where he occupied another's land on supposition it was bankrupt's land, but landlord sued real tenant for

rent for part of the time occupied by trustee. In re Wiessner, 8 A. B. R. 415 (D. C. N. Y.).

92. In re Grignard Lith. Co., 19 A. B. R. 101, 158 Fed. 557 (D. C. N. Y.).

93. See ante, § 387, et seq. But it has been held that the expenses of con-

though there will not be enough left to pay more than a dividend to labor claimants.⁹⁴

In general, a receiver will not be surcharged for losses on sales while conducting the business.⁹⁵

ducting the business may not be charged upon property to the loss of a prior valid lien thereon without the lienor's consent. See to same effect where the lienor was not notified, *In re Clark Coal & Coke Co.*, 23 A. B. R. 273, 173 Fed. 658 (D. C. Pa.).

In *re Cornice & Roofing Co.*, 13 A. B. R. 585 (D. C. Ky.): "It should not be forgotten that any effort by the general creditors or by the trustee in their behalf to make profits by continuing to execute the outstanding contracts of the bankrupt was exerted solely in the interest of the general creditors. The secured creditors, to whom this was immaterial, relying upon their liens, had no interest in the venture of the trustee undertaken for the benefit of the general creditors, and without their express consent the lienors should be regarded as having put to hazard their interests in the bankrupt's assets—a hazard for incurring which they receive no consideration. True, § 2, cl. 5, Bankruptcy Act, as it was in force in June, 1902, gave the court power to authorize a trustee to conduct, for a limited period, the business of the bankrupt; but I am much inclined to think that a referee should never permit a procedure for the carrying into effect of the unexecuted contracts of a bankrupt, to be commenced upon the initiative of the trustee. Much abuse of the power might be avoided and temptation for the trustee removed by putting that burden on the creditors. Such authorization should generally be made upon the application of some or all of the general creditors. It should never be made, if carrying it into full effect would be at the expense of secured creditors who have no interest in the question and who make no request for such authority. Indeed, the claims of secured creditors should, if possible, be fully paid or provided for before the trustee or the general creditors are permitted, except in a very small way, to embark in any venture of that sort. Of course, after the secured creditors are paid, the general creditors are in practical control of the estate, and if willing to take risks, may be indulged by the referee in proper instances, for they alone are concerned. But whether these general views are sound or not as to the

proper course to be pursued by the referee in such cases, another course was in fact pursued here, though with unfortunate results. I think it was the duty of the trustee, under the circumstances disclosed in this case, to have clearly brought before the referee the fact that his expenditures were trenching upon the fund upon which others claimed liens, and to have sought specific instructions in that contingency, even to the extent of bringing the question before the judge if necessary. I think his not doing this, but going on at a loss after expending everything on hand, was, to say the least, improvident and greatly to his disadvantage in the present contingency. * * * It does not at all seem to me that expenditures made at the instance either of the general creditors or of the trustee in their behalf to do what was done for their sole benefit in this instance are such 'costs of administration' as were in the contemplation of Congress when it used that phrase in the Act. Such expenditures occur in a special and abnormal case, which could hardly have been within such contemplation. The phrase has a much more restricted signification. See §§ 40, 48, 51, 52. I go further, and doubt whether the expenses of continuing the business of the bankrupt for a limited period, under § 2, cl. 5, would take priority over valid liens already existing and fixed, such as were Ronald's and Root's, Section 67, cl. 3. In my judgment valid liens, properly acquired and fixed could not be displaced by the trustee or the general creditors in any such subsequent proceeding for the sole benefit of the latter."

⁹⁴. In *re Krause*, 19 A. B. R. 93, 155 Fed. 702 (D. C. N. Y.).

⁹⁵. In *re Isaacson*, 23 A. B. R. 98, 174 Fed. 406 (C. C. A. N. Y.). Also, compare, *In re Consumer's Coffee Co.*, 20 A. B. R. 835, 162 Fed. 786 (D. C. Pa.); also, compare, *In re Bayley*, 22 A. B. R. 249, 177 Fed. 522 (D. C. Pa.).

Likewise, receiver conducting business at a loss without keeping proper books, and leaving bankrupt's officers in charge, and commingling funds of estate with his own funds—part of loss surcharged upon his account, *In re*

To what extent a receiver or trustee may buy from a corporation or firm in which he is interested is largely dependent on the particular circumstances.⁹⁶

§ 2037. Auctioneer.—Where special necessity exists for the employment of an auctioneer, his compensation may be allowed.⁹⁷

But the employment of an "official" auctioneer to act in all cases would seem to be improper. The selling of the property is one of the ordinary duties of the trustee; and to compel all sales to be made through one channel is clearly contrary to the spirit of the Bankruptcy Act. The trustee's individual skill is set at naught, and the creditors' selection to that extent defeated.⁹⁸

But the practice in some districts tends to have official receivers and "official" auctioneers as the general rule. The Bankruptcy Act seems in its spirit opposed to such "official" personages.⁹⁹

§ 2037½. Employing Agents to Procure Purchasers.—In a special case it is undoubtedly within the discretion of the court to authorize the employment of real estate brokers or other agents to aid in procuring purchasers, though in general the obtaining of purchasers is one of the ordinary business duties of the trustee. Such employment will not be reviewed except for abuse of discretion. Yet such employment is liable to lead to serious abuses.¹ A mere volunteer may not be allowed commissions as agent or broker, even though his services be beneficial.²

§ 2037½. Expert Accountant.—In special instances it may be proper for the trustee to employ an expert accountant, to investigate the bankrupt's books, etc.³

§ 2038. Premium on Bond.—The premium charged by a surety com-

Consumer's Coffee Co., 20 A. B. R. 835, 162 Fed. 786 (D. C. Pa.).

Suing receivers or trustees for acts done while conducting business, see ante, §§ 1780, 1780½, 1783, 1784.

Running of hotel by trustee pending sale—whether trustee may be surcharged for permitting liens for supplies to acquire precedence over landlord's lien, *In re Bayley*, 22 A. B. R. 249, 177 Fed. 522 (D. C. Pa.).

Compensation where case transferred from one District Court to another, *In re Isaacson*, 23 A. B. R. 98, 174 Fed. 406 (C. C. A. N. Y.).

No collateral attack on order to continue business, *In re Isaacson*, 23 A. B. R. 98, 174 Fed. 406 (C. C. A. N. Y.).

^{96.} Instance, *In re Frazin & Oppenheim*, 24 A. B. R. 598, 181 Fed. 307 (C. C. A. N. Y.), quoted at § 384¾.

^{97.} See ante, § 1934.

^{98.} But compare, *In re Meyer Benjamin*, 13 A. B. R. 18 (D. C. N. Y., affirmed, on review, in 14 A. B. R. 481): The abuses mentioned in Judge Holt's opinion, as the same appears in the opinion of the C. C. A., on review of the case *In re Benjamin*, 14 A. B. R. 481, ought to be met by a better remedy.

^{99.} Inferentially, Gen. Order No. XIV (1): "No official trustee shall be appointed by the court, nor any general trustee to act in classes of cases."

^{1.} *Gold v. South Side Trust Co.*, 24 A. B. R. 578, 179 Fed. 210 (C. C. A. Pa.), quoted at § 3011½.

^{2.} *Gold v. South Side Trust Co.*, 24 A. B. R. 578, 179 Fed. 210 (C. C. A. Pa.), quoted at § 3011½.

^{3.} Instance, where refused compensation out of estate, because employment not authorized and fees exorbitant, *In re Marks*, 22 A. B. R. 54 (Ref. Ga.).

pany for becoming surety on the receiver's and trustee's bonds, is a doubtful item of expense to tax as part of the costs, unless permitted by rule of court.

Obiter, In re Hoyt, 9 A. B. R. 574, 119 Fed. 987 (D. C. N. Car.): "Prior to the act of congress giving the privilege of giving bonds in surety companies (a modern convenience), such a thing as a fee for bondsmen was unheard of as costs. There is no act making it taxable as costs, and, while courts may have allowed such costs to prevailing parties litigant, it is a new departure, and has not yet become the rule of court."

However, it has been held to be a proper charge against the estate; and such would appear to be the rule now fairly established.⁴

§ 2039. Not Necessary to Pay Expenses Out of Pocket First, Then to Be Allowed Reimbursement.—Neither the receiver nor trustee in bankruptcy is required first to pay his expenses out of his own pocket, and then be allowed reimbursement therefor out of the estate.

In re McKenna, 15 A. B. R. 9, 137 Fed. 611 (D. C. N. Y.): "This court is aware of the rule which has been adopted in some of the State courts that no allowance will be made for legal services until the executor or administrator or other trustee has first paid therefor; that then he may present the bill in his account, and ask reimbursement. This rule always leaves the trustee, executor or administrator open to have the propriety of his allowance and payment questioned by those interested in the fund. If the court decides that he has paid too much, he must stand the loss, for he has undertaken to decide that matter for himself, and, having conceded the justice of the claim of the attorney—their claim being a personal one against him—he is without remedy. Without questioning the wisdom or propriety or justice of such a rule in the cases where it has been applied by the State courts, this court is decidedly of the opinion that it ought not to prevail in the bankruptcy court. Here there are meetings of the creditors, where all parties in interest may come before the court. The attorneys who have rendered services for the trustee or for the receiver in bankruptcy may come before the court or referee, as the case may be, and present their claim. If no objection is made by any party, and the court or referee in bankruptcy deems the bill reasonable for the services rendered, it may be allowed, and payment directed from the estate. It is entirely immaterial to those in interest whether the compensation going to attorneys for the trustee be first paid by the trustee personally, from his own funds, or by the trustee, under an order of the court, direct to the parties entitled thereto, from the estate, provided it is allowed by the court after a fair hearing. The practice adopted in this case relieved the trustee from the imputation of having undertaken to decide as to the compensation his attorneys ought to receive from the estate. The course pursued left it entirely to the court or referee in bankruptcy to determine the necessity and the value of the services rendered. This practice has been many times approved in the bankruptcy court, and is approved by this court. In the opinion of this court, neither a trustee nor a receiver in bankruptcy ought to be permitted to pay money of the estate to his attorneys or counsel without the order or authority of the court, and certainly such officers ought not to be required to pay for

4. In re Lunch Co., 25 A. B. R. 612 (Sp. M. N. Y.).

such services from their own funds. It is always, however, within the power of a receiver or trustee to pay the attorney from his own funds, and then ask reimbursement from the estate by order of the court."

§ 2039¹/₂. Receivership Expenses on Dismissal of Petition.—Where there is no adjudication it would appear that there is not such an "administration" of the estate, notwithstanding the decision of the Supreme Court in *Cameron v. United States*,⁵ as will permit the expenses of the receivership being charged out of the assets, unless in exceptional circumstances.

In *re Wentworth Lunch Company*, 27 A. B. R. 515, 191 Fed. 821 (C. C. A. N. Y.): "And as a corollary to the conclusion that the District Court had jurisdiction of the controversy, it follows that it had power to appoint the receiver. But it does not follow that the expenses of the bankruptcy receivership should be paid out of the property of the corporation, which was not subject to the Bankruptcy Act, rather than by the defeated parties who instituted the proceedings and obtained the appointment of the receiver. There is nothing in the record to show that it was 'absolutely necessary' for the preservation of the estate that a receiver should be appointed. The property was already in the custody of an assignee under State laws and presumably he would do his duty. Nothing is shown to justify the appointment of a receiver within the principles recently laid down by this court in *Matter of Oakland Lumber Company* (C. C. A., 2d Cir.), 23 Am. B. R. 181, 174 Fed. 634, 98 C. C. A. 388. Moreover, the question whether this corporation was subject to the bankruptcy law was obviously a doubtful one when the petition was filed and it was immediately raised. It was peculiarly a case in which a receiver should not have been appointed unless imperatively required. We find no such imperative necessity and think that the creditors who rushed in and insisted upon an unnecessary receivership should pay the expenses rather than that they should be charged upon the corporation which, as the event proved and as it always insisted, should not have been haled into the bankruptcy court at all."

However, where the receivership was absolutely necessary for the preservation of the estate and was a benefit even had there been no bankruptcy petition filed, then, in the discretion of the court, such expenses perhaps might be charged against the estate; as, for instance where the petition was defeated solely upon the ground that the debtor was insane, there being necessity for some custodian to take charge, in any event.⁶

§ 2040. Costs and Expenses of Litigation.—Costs and expenses of litigation in recovering and defending the possession of property and in contesting claims are proper charges, when necessary.⁷

§ 2041. Attorney's Fees Incurred by Trustees and Receivers.—Legitimate expenses of the receiver and trustee may include attorney's fees.⁸

5. Quoted at § 1543.

6. In *re Ward*, 29 A. B. R. 547, 194 Fed. 174 (D. C. N. J.). Also compare §§ 398 and 398¹/₄.

7. Trustee refused reimbursement for expenses in carrying up review of judge's adverse ruling, because of

laches, etc. In *re Josephson*, 9 A. B. R. 608, 121 Fed. 142 (D. C. Ga.).

8. Page *v. Rogers*, 17 A. B. R. 854, 149 Fed. 194 (C. C. A. Tenn.); In *re Oppenheimer*, 17 A. B. R. 59 (D. C. Pa.); In *re Hitchcock*, 17 A. B. R. 664 (D. C. Hawaii); *Davidson v. Friedman*,

SUBDIVISION "C."

ATTORNEYS' FEES IN BANKRUPTCY PROCEEDINGS.

§ 2042. **Allowable Attorneys' Fees.**—Reasonable attorneys' fees may be allowed out of the estate, to the petitioning creditors and the bankrupt by express statutory provision, and to the trustee and receiver as part of their expenses.

One of the most vexatious problems in the practical administration of bankrupt estates is the determination of the propriety and amount of attorneys' fees allowable out of the estate.

§ 2043. **Clerical Work and Ordinary Business Advice Not to Be Charged for at Professional Rates.**—The fees charged for at professional rates must be for professional services; not for clerical work nor for ordinary business advice or work.⁹

In *re Connell & Sons*,⁹ 9 A. B. R. 475, 120 Fed. 846 (D. C. Pa.): "But it is not so much what was done by the attorney, as what was really required. The bankrupts are responsible individually to the extent that they employed him, regardless of the character of what he was called upon to do, but not so the estate. This is a preferred claim, and is to be kept down to what it was intended by the act to represent, and that is simply the necessary professional assistance required by the bankrupts to meet the demands of the act upon them. In the present instance, the time spent seems to have been mainly taken up in going over the books of the firm and straightening them out by posting and otherwise. A part of this may be regarded as necessary, but part certainly was not. It was the work of a bookkeeper or an accountant rather than a lawyer to post the books and reduce them to the condition where the information they contained would be available and for this no claim can be made. Neither can there for the writing up of the extra copies of the schedules after the first one had been made out. This was mere clerical work, which any one could do who wrote a fair hand, and is not to be charged against the estate at professional rates."

A considerable portion of the work in bankruptcy administration commonly charged for at professional rates is really clerical work. Thus, a goodly part of the preparation of the bankrupt's schedules is purely clerical work that should not be estimated at professional rates;¹⁰ although, to be sure, genuine professional advice in the preparation may also be requisite, in the classification of assets, liabilities, etc., and in pointing out the proper forms.¹¹

15 A. B. R. 489, 140 Fed. 853 (C. C. A. Mich.). For discussion of this expense, see the general discussion of attorney's fees in the next division—Division 4.

As to whom to employ as attorney, see ante, § 377, note.

As to "compensation" of receiver and trustee, see post, § 2108, et seq.; § 2118, et seq.

9. In *re Mayer*, 4 A. B. R. 241, 101 Fed. 695 (D. C. Wis.); In *re Lane Lumber Co.*, 30 A. B. R. 749, 206 Fed. 780 (D. C. Idaho).

10. In *re Lane Lumber Co.*, 30 A. B. R. 749, 206 Fed. 780 (D. C. Idaho).

11. In *re Terrill*, 4 A. B. R. 625, 103 Fed. 781 (D. C. Vt.).

§ 2044. For Many Services Attorney to Seek Pay from Own Client, Not from Estate.—For many of the services ordinarily performed, the attorney must seek his pay from his own client, rather than from the estate.¹²

In *re Rozinsky*, 3 A. B. R. 831, 101 Fed. 229 (D. C. N. Y.): "In the present case it is manifest that the examination was conducted in the interest of the general creditors. The trustee was elected by the attorney of those creditors, and the latter was in turn immediately employed by the trustee in an uncertain search after assets. The funds in hand necessary to pay preferred claims should not be thus depleted, but such services should be regarded as virtually in behalf of the creditors who are the clients of the attorney, and upon the credit of what they may succeed in realizing."

And charge must not be made out of the estate for services really performed for particular creditors represented by the attorney.¹³

§ 2045. Fees Must Be "Reasonable."—The fees allowed must be reasonable. What is and what is not a reasonable fee in bankruptcy has been touched upon by the decisions in numerous instances.¹⁴

¹² In *re Connell & Sons*, 9 A. B. R. 475, 120 Fed. 846 (D. C. Pa.). Instance, In *re Castleberry*, 16 A. B. R. 430, 143 Fed. 1021 (D. C. Ga.): Thus the bankrupt in having his exemptions allowed. In *re Hart & Co.*, 16 A. B. R. 726 (D. C. Hawaii): Petitioning creditors for preliminary consultations before decision to file bankruptcy petition. Instance, In *re Oppenheimer*, 17 A. B. R. 60 (D. C. Pa.). Instance, In *re Coventry Evans Furn. Co.*, 22 A. B. R. 623, 166 Fed. 516, 171 Fed. 673 (D. C. N. Y.); mortgagee allowed to foreclose out of bankruptcy court. Instance, In *re Claussen*, 21 A. B. R. 34, 164 Fed. 300 (D. C. S. Car.). Impliedly, In *re Lane Lumber Co.*, 30 A. B. R. 749, 206 Fed. 780 (D. C. Idaho); *Eichholz v. Polack*, 25 A. B. R. 243, 140 App. Div. N. Y. 551; In *re Gillaspie*, 27 A. B. R. 59, 190 Fed. 80 (D. C. W. Va.).

¹³ In *re Ketterer Mfg. Co.*, 19 A. B. R. 646, 156 Fed. 719 (D. C. Pa.).

¹⁴ In *re Covington*, 13 A. B. R. 150, 132 Fed. 884 (D. C. N. Car.): Allowance of \$200 to petitioning creditors' attorney and \$50 to bankrupt's attorney, in an estate of \$2000.

In *re Silverman & Schoor*, 3 A. B. R. 227 (D. C. N. Y.): Petitioning creditors allowed \$75.00 on an uncontested petition and for obtaining stay of pending litigation.

In *re Goldville Mfg. Co.*, 10 A. B. R. 552, 123 Fed. 579 (D. C. S. C.): Petitioning creditors' attorney in estate of \$2,800 allowed \$250.

In *re Smith*, 5 A. B. R. 559, 108 Fed.

89 (D. C. N. Car.): Voluntary bankrupt's attorney allowed \$50.

In *re Carr*, 8 A. B. R. 635, 117 Fed. 572 (D. C. N. Car.), where the court refused to follow the recommendation of the referee, regarding it exorbitant.

In *re Connell & Son*, 9 A. B. R. 474, 120 Fed. 846 (D. C. Pa.): In voluntary case bankrupt's attorney allowed \$100.

Smith v. Cooper, 9 A. B. R. 755, 120 Fed. 230 (C. C. A. Ga.), wherein the circuit court of appeals restored the master's recommendation of \$1,000 which the district court had cut down.

In *re Rozinsky*, 3 A. B. R. 831, 101 Fed. 229 (D. C. N. Y.): Attorney for trustee refused allowance for uncertain chase after alleged concealed assets where done at expense of labor claimants.

In *re Lang*, 11 A. B. R. 794, 127 Fed. 755 (D. C. Tex.): Cutting down allowance to bankrupt's attorney in a voluntary case to \$75, the estate being \$7,500.

In *re O'Connell*, 3 A. B. R. 422, 98 Fed. 83 (D. C. N. Y.): Allowance to bankrupt refused for attorney's fees out of fraudulently conveyed property recovered by trustee.

In *re Felson*, 15 A. B. R. 185, 139 Fed. 275 (D. C. N. Y.): Allowance of \$50 to bankrupt's attorney in an estate of \$4,656 for schedules and examination.

In *re Mayer*, 4 A. B. R. 239, 101 Fed. 695 (D. C. Wis.): \$25 to \$50 for preparation of schedules.

In *re Martin-Borgeson Co.*, 18 A. B. R. 179, 151 Fed. 780 (D. C. N. Y.): \$150

§ 2046. "Reasonableness" Left to Sound Judicial Discretion of Court.—What is a reasonable amount for an attorney's fee in bankruptcy

for receiver's attorney in estate of \$4,600.

In re Byerly, 12 A. B. R. 188, 128 Fed. 637 (D. C. Penn.): Disallowing any attorney fee at all for trustee on account of the small size of the estate and lack of necessity for employment.

In re Curtis, 4 A. B. R. 17, 100 Fed. 784 (C. C. A. Ills.): In estate of \$102,000 allowance of \$12,500 to petitioning creditors excessive; \$2,000 proper allowance.

In re Kross, 3 A. B. R. 187, 96 Fed. 816 (D. C. N. Y.): Allowance to bankrupt's attorney of \$30 for petition, schedules, etc., and \$20 for discharge.

In re Terrill, 4 A. B. R. 625, 103 Fed. 781 (D. C. Vt.): Bankrupt filling out his own petition and schedules.

In re Morris, 11 A. B. R. 145, 125 Fed. 841 (D. C. N. Car.): "This court has, by rule, fixed the maximum fee in voluntary proceedings, where there is no unforeseen litigation or extraordinary services, at \$50."

In re Lewin, 4 A. B. R. 632, 103 Fed. 850 (D. C. Vt.): Re-examination of prepayment of \$82.50 to bankrupt's attorney.

In re Oppenheimer, 17 A. B. R. 60 (D. C. Pa.): Receiver's attorney fee \$100 in an estate of \$4,200.

In re Anderson, 4 A. B. R. 640, 103 Fed. 854 (D. C. S. C.): Allowance of \$90 to involuntary bankrupt's attorney.

In re Mercantile Co., 2 A. B. R. 419, 95 Fed. 123 (D. C. Mo.): Nor to exceed \$50 to petitioning creditors' attorneys in default cases, for all work including schedules, where ordered; and \$25 additional for pro forma injunction against transfer of assets by trustee or assignee.

In re Little River Lumber Co., 3 A. B. R. 685, 101 Fed. 558 (D. C. Ark.); In re Tebo, 4 A. B. R. 235, 101 Fed. 419 (D. C. W. Va.); In re Smith, 1 A. B. R. 37 (Ref. N. Y.); In re Mitchell, 1 A. B. R. 665, 93 Fed. 803 (Ref. Wis.); In re Mitchell, 1 A. B. R. 687 (Ref. Pa., disapproved in In re Felson, 15 A. B. R. 193, 139 Fed. 275); In re Stotts, 1 A. B. R. 641, 93 Fed. 438 (D. C. Iowa); In re Frick, 1 A. B. R. 719 (Ref. Ohio); In re Smith, 2 A. B. R. 648 (Ref. N. Y.): Percentages adopted.

In re Woodard, 2 A. B. R. 692, 95 Fed. 955 (D. C. Va.): \$75 allowed to petitioning creditors.

In re Burrus, 3 A. B. R. 296, 97 Fed. 926 (D. C. Va.): Voluntary bankrupt's

attorney allowed \$200: injunctions being obtained, etc.

In re Fletcher, 10 A. B. R. 400 (Ref. N. Y.): Allowance refused to creditors' attorney for contesting claims before election of trustee.

In re Evans, 8 A. B. R. 730, 116 Fed. 909 (D. C. N. Car.): Allowance refused to trustee who was attorney.

In re Stratemeyer, 14 A. B. R. 121 (D. C. Hawaii): \$50 allowed bankrupt's attorney for schedules, examination and discharge.

In re Brundin, 7 A. B. R. 298, 112 Fed. 306 (D. C. Minn.): Bankrupt's attorney allowed \$271.00.

In re Rosenthal & Lehman, 9 A. B. R. 626, 120 Fed. 848 (D. C. Mo.): Allowance refused because no showing of necessity made.

Liddon & Bro. v. Smith, 14 A. B. R. 204, 135 Fed. 43 (C. C. A. Fla.): Allowance refused.

In re Abram, 4 A. B. R. 575, 103 Fed. 272 (D. C. Calif.).

In re Niman, 14 A. B. R. 515 (Ref. Mich.): Estate apparently only worth \$1,400: vigorous action of attorney discovered and recovered \$16,000: court allowed \$2,500 for attorney's fees.

In re Talton, 14 A. B. R. 617, 137 Fed. 178 (D. C. N. Car.): Bankrupt's and petitioning creditors' attorneys' fees in cases of composition: \$20.00 allowed to bankrupt's attorney and \$50 to petitioning creditors.

In re McKenna, 15 A. B. R. 4, 137 Fed. 611 (D. C. N. Y.): \$800 to attorneys for trustee where controversy involved netted \$20,000 to estate, and time consumed was 50 days; and amount realized paid all debts.

In re Carolina Cooperage Co., 3 A. B. R. 154, 96 Fed. 950 (D. C. N. Car.): Bankrupt's attorney fee reduced from \$75 to \$25.

In re Kelly Dry Goods Co., 4 A. B. R. 528, 102 Fed. 747 (D. C. Wis.).

Page v. Rogers, 17 A. B. R. 854, 149 Fed. 194 (C. C. A. Tex.): \$15,000 allowed in an estate of \$71,000, where total indebtedness was about \$78,000.

In re Ketterer Mfg. Co., 19 A. B. R. 646, 156 Fed. 719 (D. C. Pa.). Receiver's attorney allowed \$1,500.

In re Lane Lumber Co., 30 A. B. R. 749, 206 Fed. 780 (D. C. Idaho). Bankrupt's attorney's fee bill of \$1850 for attendance at examination cut down to \$100 where no showing was made of having been ordered to appear at examination nor necessity therefor;

is left to the sound judicial discretion of the court, but not its unrestrained discretion.¹⁵

In *re Curtis*, 4 A. B. R. 17, 100 Fed. 784 (C. C. A. Ills.): "So, also, the amount to be allowed does not rest in mere discretion. The amount must in all cases be reasonable, to be determined upon evidence of the service performed and of its value, and, in the absence of evidence of its value, by the court from knowledge of its worth."

And the order of allowance of attorneys' fees is subject to review.¹⁶

Their fees must be reasonable fees, but there is great diversity of mind among lawyers as to the method of arriving at the reasonableness of attorney's fees. It is sometimes said that the customary, and hence reasonable, attorney's fee is a certain fixed amount per day; but certainly such cannot be a correct rule, else it is continually disregarded in practice. Neither attorneys nor litigants take a fixed amount per day as the criterion of the reasonableness of any certain charge for attorney's fees; and what common consent acquiesces in is likely to be reasonable. Thus, it would

charge of \$750 for preparing schedules being also cut down to \$285.

In *re Duran Mercantile Co.*, 29 A. B. R. 450, 199 Fed. 961 (D. C. N. Mex.): \$50 for preparing and filing schedules and other papers necessary to the adjudication; \$25.00 for attending the bankrupt before referee and \$25.00 for securing a stay order of prosecution in the state court.

In *re Kyte*, 19 A. B. R. 768, 158 Fed. 121 (D. C. Pa.): Receiver's attorney's fee cut down from \$200 to \$150.

Ohio Valley Bank Co. v. Mack, 20 A. B. R. 919, 163 Fed. 155 (D. C. Ohio): No fee allowed receiver, he being a lawyer.

In *re Irwin*, 23 A. B. R. 487, 174 Fed. 642 (C. C. A. Pa.): Increasing bankrupt's attorney's fees from \$37.50 to \$100 in an estate of at least \$2,074.

Ohio Valley Bank Co. v. Mack, 20 A. B. R. 919, 163 Fed. 155 (D. C. Ohio): \$150 allowed petitioning creditors.

In *re Southern Steel Co.*, 22 A. B. R. 476, 169 Fed. 702 (D. C. Ala.): \$5,000 allowed to petitioning creditors' attorneys.

In *re Fidler & Son*, 23 A. B. R. 16, 172 Fed. 635 (D. C. Pa.): Attorney allowed \$250 where his vigorous action resulted in bringing into the estate \$500.

In *re Hoffman*, 23 A. B. R. 19, 173 Fed. 234 (D. C. Wis.), where, in a proceeding against a bankrupt's wife, who was suspected of having appropriated and concealed some \$6,000 worth of assets, the attorneys for the trustees were allowed \$1,500 on account of services rendered in the litigation, a

finding of the referee upon the attorneys' application for an additional allowance of \$1,000, that the original allowance was sufficient, the litigation having resulted in no benefit to the estate, will be affirmed, but his finding disallowing the attorney's claim for actual disbursements, certified to have been proper, was reversed.

Ohio Valley Bank Co. v. Mack, 20 A. B. R. 919, 163 Fed. 155 (D. C. Ohio): No allowance until itemization of services made, trustee himself being an attorney.

Ohio Valley Bank Co. v. Mack, 20 A. B. R. 919, 163 Fed. 155 (D. C. Ohio): Bankrupt's attorney in involuntary case allowed \$25 for preparing schedules, etc.

In *re Berkowitz*, 22 A. B. R. 236 (Ref. N. J.), \$5,000 allowed attorneys for petitioning creditors and trustee, in estate of \$17,362.54, where schedules set forth no assets and entire estate the result of able and vigorous legal work.

15. *Smith v. Cooper*, 9 A. B. R. 755, 120 Fed. 230 (C. C. A. Ga.); In *re Young*, 16 A. B. R. 108, 142 Fed. 891 (D. C. N. Car.); In *re Hill Co.*, 20 A. B. R. 73, 159 Fed. 73 (C. C. A. Ills.).

16. *Smith v. Cooper*, 9 A. B. R. 755, 120 Fed. 230 (C. C. A. Ga.). Instance, *Page v. Rogers*, 17 A. B. R. 855, 149 Fed. 194 (C. C. A. Tenn.); In *re Irwin*, 23 A. B. R. 487, 174 Fed. 642 (C. C. A. Pa.).

No formal exceptions are requisite. Compare § 2845. Also see In *re Lane Lumber Co.*, 30 A. B. R. 749, 206 Fed. 780 (D. C. Idaho).

hardly be right to charge \$25 per day for instance, for services in a suit involving only a few dollars, else poor people never could get their rights; nor, on the other hand, would it be reasonable for lawyers in a great case to be restricted to \$25 per day. Other elements are to be taken into account besides merely the time involved.

§ 2047. Various Elements to Be Considered, Each Having Modifying Effect.—The time alone used by the attorney is not the only standard whereby to measure the reasonableness of the fees. There are at least five elements in all: The time properly to be spent on the particular controversy involved;¹⁷ the intricacy of the questions involved therein; the amount involved in that controversy;¹⁸ the strenuousness of the opposition encountered; and the results achieved therein.¹⁹

In *re McKenna*, 15 A. B. R. 10, 137 Fed. 611 (D. C. N. Y.): "In fixing the value of legal services, courts have many things to consider—the nature and importance of the business transacted; the ability of the parties to pay; the amount of the estate involved; the magnitude of the interests in question; the standing and ability of the attorneys employed; the location of the parties and of the attorneys. These and many other things are proper subjects of consideration."

In *re Goldville Mfg. Co.*, 10 A. B. R. 559, 123 Fed. 579 (D. C. S. C.): "The amount of the estate must to a large extent govern its discretion in determining what is 'reasonable.'"

Ward v. Kohn (C. C. A.), 58 Fed. 462: "In the absence of a contract price, attorneys are entitled to receive what they deserve for their services. The amount of their compensation must vary with the place in which their services are rendered, for the same services are of more value in a large and prosperous commercial city than in a small country town; with the character and standing of the lawyer who renders them, for the services of an attorney of ripe experience, great learning, eminent ability, and high reputation deserve and command better compensation than those of the tyro in the profession; with the importance of the matters involved in the litigation, for the same service deserve more compensation where life, liberty, character, or large amounts of property are at stake than where but a few dollars are in dispute; and with the results attained, for success earns a better reward than failure.

"The wealth of a defendant cannot be considered in any case to enhance the fee for professional services above a reasonable compensation for the service actually rendered. It cannot be considered to make a fee extortionate or a compensation unreasonably large. But every judge and every gentle-

17. In *re Lane Lumber Co.*, 30 A. B. R. 749, 206 Fed. 780 (D. C. Idaho).

18. In *re Ellett Electric Co.*, 28 A. B. R. 453, 196 Fed. 400 (D. C. N. Y.).

19. In *re Berkowitz*, 22 A. B. R. 236 (Ref. N. J.); In *re Ellett Electric Co.*, 28 A. B. R. 453, 196 Fed. 400 (D. C. N. Y.); In *re Fiske & Co.*, 31 A. B. R. 736, 209 Fed. 982 (D. C. N. Y.); In *re Knight*, 3 N. B. N. & R. 446 (Ref. Ohio). See note, In *re Smith*, 5 A. B. R. 559, to be found on page 560. Also, to similar effect, *Smith v. Cooper*,

9 A. B. R. 758, 120 Fed. 230 (C. C. A. Ga.).

Maximum Fixed by Local Rule in Southern District of New York.—In the Southern District of New York by local rule referees may not allow to attorneys for the trustee and receiver respectively more than twice the amount received in that particular case by the receiver or trustee. The judge by special order may allow more. In *re Keller*, 31 A. B. R. 51, 207 Fed. 118 (D. C. N. Y.).

man of the bar knows that much severe professional labor is rendered by practicing attorneys without any compensation, and much more for compensation so small as to be entirely inadequate. It is as difficult to defend the poor as the rich from a groundless charge of murder. It requires as much learning, labor, and professional skill to recover or save from attack property of little value, that may be the entire estate of the poor man, as it does to recover thousands of dollars for the wealthy. The duty of the lawyer to defend the former and maintain his rights is as great as it is to the latter, and to the honor of the profession it may be said that it is performed with equal zeal and fidelity. But it is the general practice of the gentlemen of the bar to fix the fees for such services far below a fair compensation or to charge no fee at all—to measure their fees more by the inability of such a client to pay a fair compensation, or to pay at all, than by the value of the services they render. When, on the other hand, a client, who has the means to pay what professional services are fairly worth, employs an attorney, it is right and just that he should pay a fair and reasonable compensation for the service he obtains. In other words, the fees the attorney deserves from such a client should not be measured by the inadequate compensation and small fees the gentlemen of the bar usually receive from those who are unable to pay at all or to pay a fair compensation, but they should be measured by the fees usually obtained by attorneys for like services from those who are able to pay just compensation for the service rendered."

Compare, to similar effect, *In re Lang*, 11 A. B. R. 794, 127 Fed. 755 (D. C. Tex.): "It may not always be an easy matter to determine the exact value of the services of an attorney. Such value varies, as the value of the surgeon's work varies with the importance of the operation and the skill and delicacy required in performing it. Where the operation is simple and relatively unimportant, the fee exacted would be small in comparison with that demanded for more serious work. So it is with the services of the attorney, and no fixed, absolute fee can be provided for all cases. The amount of compensation should be based, in ordinary cases, upon the nature of the case, the extent and character of the work actually performed, and the amount involved in the controversy."

Compare, to similar effect, *In re Curtis*, 4 A. B. R. 19, 100 Fed. 784 (C. C. A. Ills.): "The elements which enter into and should control judgment upon the value of professional services we think to be these: The nature of the service, the time necessarily employed therein, the amount involved, the responsibility assumed, and the result obtained."

In re Burns, 3 A. B. R. 296 (D. C. Va.): "* * * the character of the estate, its condition at the time of the adjudication, the injunctions or restraining orders necessary to be secured for its protection, and the corresponding amount of time and care required of the petitioner's attorney, are all matters to be considered by the court in arriving at the amount 'reasonable' under the circumstances. Necessarily, therefore, there can be no fixed and determinate fee for all cases, nor will the amount allowed in this case establish a rule for subsequent cases in this court, but from a careful consideration of the evidence certified by the referee herein the court deems \$200, in addition to the \$45.45 already allowed and paid for expenses incurred, a reasonable fee, and the order of the referee will be modified accordingly."

There is sometimes another element added, namely, the "dignity" and "standing" of the attorney himself.²⁰ This element, however, seems at least undignified: justice and fairness, it would seem, would resolve the value

20. *In re McKenna*, 15 A. B. R. 10, 137 Fed. 611 (D. C. N. Y.).

of the "dignity" and "standing" of the attorney in any particular case into one or the other of these five elements above laid down. "Dignity" should not be paid for, but the work accomplished in view of all the circumstances and questions involved rather should control.

But it is undoubtedly proper to consider, as an element, the vigor of the opposition; for a controversy in itself involving propositions of small merit may be rendered vexatious by the strenuousness of one's adversaries.²¹

The results achieved through the efforts of the attorney also have an important bearing upon the reasonableness of the allowance.²²

In re [Francis Levy] Outfitting Co., 29 A. B. R. 8 (D. C. Hawaii): "With the testimony that, considering purely the care and time involved, the services are worth \$250, I do not agree—at least in any practical view; for such fees must depend upon the condition of the estate, as one of the main considerations, i. e. upon the results effected, the assets saved."

Again, the intricacy of the legal questions involved should be taken into account.

Inferentially, In re Curtis, 4 A. B. R. 20, 100 Fed. 784 (C. C. A. Ills.): "This was the nature of the service that was rendered, and involved the investigation and discussion of the questions whether a voluntary assignment, after the passage of the bankrupt law was void, or voidable merely, of the doctrine of estoppel in pais, and of the election of remedies. These questions were important, requiring careful study and legal ability for their proper presentation to the court."

Inferentially, In re Oppenheimer, 17 A. B. R. 60, 146 Fed. 140 (D. C. Pa.): "* * * so there was no great responsibility involved in its management, nor any intricacy in advising with regard to it, both of which bear on the value of the services rendered and the amount to be allowed."

Each of these elements has a modifying effect upon all the others, to increase or decrease the fees to be allowed, as the case may be. Thus, where the issues raised are uncontested or are practically incontestible, there would be a corresponding tendency toward reduction of the fees. Again, petitioning creditors would not be entitled to as great an allowance for attorneys' fees where an assignment for the benefit of creditors, or a written admission of inability, etc., is the act of bankruptcy alleged, as they would where an act of bankruptcy more difficult of proof and more likely to be contested and to require preparation for trial, is set up.²³

²¹ In re Francis, etc., Co., Ltd., 29 A. B. R. 8 (D. C. Hawaii).

²² Instance, In re Niman, 14 A. B. R. 515 (Ref. Mich.): In this case the court allowed \$2,500 where, in an estate of apparently only \$1,400 the vigorous action of the attorney resulted in the recovery of \$16,000.

Instance, In re Berkowitz, 22 A. B. R. 236 (Ref. N. J.): \$5,000 allowed attorneys in an estate of \$17,000, where the bankrupt's schedules originally

showed no assets and entire estate result of attorney's vigorous work in uncovering the fraud of an alleged corporation formed to aid bankrupt to conceal assets; instance, In re Fidler & Son, 23 A. B. R. 16, 172 Fed. 635 (D. C. Pa.) where, though fine work was done, the pecuniary benefit to the estate was not very great.

²³ In re Silverman & Schoor, 3 A. B. R. 227 (D. C. N. Y.). Instance, In re Carolina Cooperage Co., 3 A. B. R. 157, 96 Fed. 604 (D. C. N. Car.).

It is also perhaps proper to take into account the locality: since, after all, compensation is to a certain degree regulated by the comparative standard or cost of living. Thus, the same services in the same litigation might merit different compensation to the attorney in a city where the cost of living is high from what the same attorney should expect were he a resident of a place where the cost of living is comparatively low.

The fact that more than one attorney was employed is not to be considered as an element in arriving at the amount of attorney's fee allowable out of bankrupt estates but the allowance should be made as though only one attorney were employed.²⁴

§ 2048. Sixth Element, in Bankruptcy Cases, "Economy."—And in bankruptcy the policy of the act towards strict economy should be kept in view.²⁵

In *re Goldville Mfg. Co.*, 10 A. B. R. 556, 123 Fed. 579 (D. C. S. C.): "It is a part of the history of the country that one of the causes which led to the repeal of the Bankrupt Act of 1867 * * * was the great abuse, under the former law, whereby the estates of bankrupts were consumed by the ministerial officers of the court in enormous costs and charges; and it was the clear intent of the present Bankrupt Law that they should be administered for the benefit of the creditors. This is manifest through all the provisions respecting fees and commissions. The compensation allowed to clerks, referees, and trustees is so meagre that it is a matter of some surprise that the courts have been able to secure persons of any competency to administer the law. Under the former act legal services rendered to the bankrupt were not allowed as a claim entitled to priority, but under the present law such claims are allowed priority in the discretion of the court; but that discretion should be exercised to carry out and effectuate the legislative will, and the courts cannot honestly disregard the manifest policy of the law, which looks to great economy of administration. If they enforce strict compliance with the statute on the part of ministerial officers with respect to such fees and allowances as are prescribed by law, they cannot refuse to be bound by its limitations in matters that are left to their discretion. That discretion must be in accordance with, and not in conflict with, the policy of the law."

24. In *re Falkenberg*, 30 A. B. R. 718, 206 Fed. 835 (D. C. N. Mex.); In *re Coney Island Lumber Co.*, 29 A. B. R. 91, 199 Fed. 197 (D. C. N. Y.), quoted at § 2065.

25. In *re Curtis*, 4 A. B. R. 17, 100 Fed. 784 (C. C. A. Ills.); In *re Mayer*, 4 A. B. R. 239, 101 Fed. 695 (D. C. Wis.); In *re Smith*, 5 A. B. R. 559, 108 Fed. 39 (D. C. N. C.); In *re Mercantile Co.*, 2 A. B. R. 419, 95 Fed. 123 (D. C. Mo.), quoted ante, § 2011; In *re Connell & Sons*, 9 A. B. R. 474, 120 Fed. 846 (D. C. Pa.), quoted ante, § 2043; *Page v. Rogers*, 17 A. B. R. 855, 149 Fed. 194 (C. C. A. Tenn.); In *re Young*, 16 A. B. R. 108, 142 Fed. 891 (D. C. N. Car.); In *re Carolina Cooperage Co.*, 3 A. B. R. 154, 96 Fed. 950 (D. C. N. Car.). See ante, § 2011, "Policy of Act,

That of Strictest Economy in the Expenses and Costs of Administration."

In *re Kyte*, 19 A. B. R. 768, 158 Fed. 121 (D. C. Pa.); impliedly, *Ohio Valley Bank Co. v. Mack*, 20 A. B. R. 919, 163 Fed. 155 (D. C. Ohio); impliedly, In *re Huddleston*, 21 A. B. R. 669, 167 Fed. 428 (D. C. Ga.); *Dunlap Hardware Co. v. Huddleston*, 21 A. B. R. 731, 167 Fed. 433 (C. C. A. Ga.); instance, In *re Fidler & Son*, 23 A. B. R. 16, 172 Fed. 635 (D. C. Pa.); In *re Duran Mercantile Co.*, 29 A. B. R. 450, 199 Fed. 961 (D. C. N. Mex.); In *re Francis, etc., Co. Lt.*, 29 A. B. R. 8 (D. C. Hawaii); In *re Lane Lumber Co.*, 30 A. B. R. 749, 206 Fed. 789 (D. C. Idaho); In *re Fullick*, 28 A. B. R. 634, 201 Fed. 463 (D. C. Pa.). See also, § 2011.

In re Rosenthal & Lehman, 9 A. B. R. 629, 120 Fed. 848 (D. C. Mo.): "And, when an allowance is made it should be remembered that the policy of the law, as disclosed in the compensation fixed for referees, clerks and trustees, is in the direction of great economy."

In re Woodard, 2 A. B. R. 339, 691, 95 Fed. 956: "One of the purposes of the Act of 1898 in establishing a uniform system of bankruptcy was to avoid what was the principal cause of the repeal of the bankruptcy Act of 1867—excessive fees and great expense."

In re Lang, 11 A. B. R. 794, 127 Fed. 755 (D. C. Tex.): "In bankruptcy cases, while these elements should properly be considered in fixing the compensation of the attorney, the policy of the act should be steadily kept in view, that is, that it should be administered with severe economy (In re Goldville Manufacturing Co., supra), so as to reduce to the lowest minimum the cost of administration."

In re Byerly, 12 A. B. R. 186, 128 Fed. 637 (D. C. Penn.): "It is the policy of the Bankrupt Act to administer the estates, which are brought into court, as economically as possible, and no large fees are to be expected. Those directly allowed by the act are purposely kept down to the lowest possible limits and the courts have no right in fixing the compensation of counsel to be differently influenced. The attorney in the present instance has received \$125 in fees and an additional \$21.76 for serving notices and mileage, the occasion for which is not altogether manifest. I agree with the referee that this is all under the circumstances that he can ask."

In re Little River Lumber Co., 3 A. B. R. 685, 101 Fed. 560 (D. C. Ark.): "In view of the whole spirit of the Bankrupt Law, counsel who are required to represent the trustee must expect only such remuneration as will actually compensate them for services rendered."

Inferentially, In re Daniels, 12 A. B. R. 450, 130 Fed. 597 (D. C. Iowa): "Much criticism was made of prior Bankruptcy Acts because of the large amount of fees and expenses incurred in the administration of the bankrupt estates. It was the manifest purpose of Congress that such criticism could not rightly be made of the present law, and it fixed the compensation of referees and other officers very low. They may be inadequate in some cases, but the court is powerless to increase them. By the amendment of February 5, 1903, it is expressly provided that the court shall not allow, under any form or guise whatever, any other or further compensation for services than that expressly authorized by the act."

In re Covington, 13 A. B. R. 150, 132 Fed. 1884 (D. C. N. Car.): "Attorneys shall be allowed reasonable compensation for services rendered which were beneficial to the estate. Beyond that point this court has never gone, and will not go in the exercise of a sound judicial discretion."

In re Oppenheimer, 17 A. B. R. 60, 146 Fed. 140 (D. C. Pa.): "Economy is strictly enjoined by the well known policy of the Bankruptcy Act, in the administration of bankrupt estates, and there is no exception with regard to the compensation of counsel."

§ 2049. Items Properly to Be Grouped According to Separate Controversies Involved and Estimate Made as to Each Group.—In determining the reasonableness of an attorney's fee bill covering services in several distinct controversies, it is convenient to group the items relating to each controversy separately and to consider the five or six elements above mentioned with relation to each group separately, rather than with

relation to the entire estate. Thus, as to the elements of the "amount involved:" in a bankruptcy case where the entire estate is, for example, \$10,000, there might exist a little controversy over a claim of merely \$100. The element of "amount involved" would be comparatively small, merely \$100, and the fees be correspondingly diminished, notwithstanding the "amount involved" in the estate as an entirety, is \$10,000.

If the bankrupt estate is free from difficult litigation or litigation involving large amounts, the creditors should receive the benefit; and the fees for services in small controversies arising in large estates should not be increased because of the size of the estate.

Again, in making allowances to petitioning creditors' and bankrupts' attorneys out of the estate, the "amount involved" is not the entire estate, where there are good and valid liens existing; but only the surplus. The adjudication is not undertaken for the benefit of the valid lienholders and does not affect them. It is for the benefit of general creditors; and the measure of the estate realized for unsecured creditors is, therefore, the measure of the "amount involved" for the purpose of determining the reasonableness of the fees for petitioning creditors' and bankrupts' attorneys.²⁶

Compare, inferentially, *In re Goldville Mfg. Co.*, 10 A. B. R. 554, 123 Fed. 579 (D. C. S. Car.): "I am of the opinion that the attorney for the petitioning creditors and the attorney for the bankrupt corporation cannot, in the circumstances, demand or receive an allowance out of the fund derived from the sale of the mortgaged property. Nothing that has been done by the petitioning creditors in the proceedings in bankruptcy was intended for or has inured to the benefit of the lien creditors. They were foreclosing their mortgage in the state court, where they had a right to be and to remain. In discontinuing their proceedings in the state court, and in filing their petition for foreclosure in this court, they have been represented by their own attorneys, and the bankruptcy proceedings have been of no benefit to them. They make no claim upon the fund in the hands of the trustee for distribution among the unsecured creditors, and it seems to the court that the unsecured creditors and their attorneys have no claim upon their fund. Section 67d of the Bankrupt Act * * * declares that: 'Liens given and accepted in good faith, etc., shall not be affected by this act.'

"Of course, all the costs of the court, and all expenses incurred in the care, preservation, and sale of the mortgaged property, are proper claims against the sum realized from the sale of it; but the fees here asked for cannot be considered as in the nature of costs of court and expenses necessarily incident to the preservation of their fund. * * *

"The claim of the attorney for the petitioning creditors rests upon what the court deems an erroneous view, that the service rendered is like that of filing a creditors' bill in chancery to marshal the assets of an insolvent estate, where assets which would otherwise have been lost are recovered, and the estate is administered for the benefit of all creditors who come in and share in the re-

26. Impliedly, *In re Frick*, 1 A. B. R. 719 (Ref. Ohio); impliedly, *Liddon v. Smith*, 14 A. B. R. 204, 135 Fed. 43 (C. C. A. Fla.). Compare, inferentially, *Frank v. Dickey*, 15 A. B. R. 158, 139 Fed. 744 (C. C. A. Mo.).

sults accomplished. In such cases courts of chancery properly considered the exacting nature of the work done, responsibility assumed and results accomplished, and may deal out compensation with a liberal hand; but in this case the mere fact of the adjudication in bankruptcy has not enabled the secured creditors to reach a fund which might otherwise have been lost. It has not added to the value of the security that they had under their mortgage, or provided them with any additional remedy. The most that can be said is that it has opened the door of this forum, where, by proceedings in rem, instituted by their own attorneys, they have secured a foreclosure of the lien which the Bankrupt Act declares 'shall not be affected by it.' They were already proceeding to foreclose their lien in another forum, where it is presumed they would have obtained equal results; and it would not seem consonant with any principle of justice, after opening the door to them, and inviting them to come in, so that the whole estate might be administered, to tax them for the payment of services not rendered at their request or for their benefit, and to deplete the fund to which they are entitled under their lien, for the compensation of an attorney who has pertinaciously, but unsuccessfully, endeavored to deprive them of it. The only fund brought into the court for administration by the bankruptcy proceedings, which otherwise would not be here, is the fund of about \$2,800 for distribution among the unsecured creditors, and this fund must be administered in accordance with the spirit of the Bankrupt Law.

"It is a part of the history of the country that one of the causes which led to the repeal of the Bankrupt Act of 1867 * * * was the great abuse, under the former law, whereby the estates of bankrupts were consumed by the ministerial officers of the court in enormous costs and charges; and it was the clear intent of the present Bankrupt Law that they should be administered for the benefit of the creditors. This is manifest through all the provisions respecting fees and commissions. The compensation allowed to clerks, referees, and trustees is so meager that it is a matter of some surprise that the courts have been able to secure persons of any competency to administer the law. Under the former act legal services rendered to the bankrupt were not allowed as a claim entitled to priority, but under the present law such claims are allowed priority in the discretion of the court; but that discretion should be exercised to carry out and effectuate the legislative will, and the courts cannot honestly disregard the manifest policy of law, which looks to great economy of administration. If they enforce strict compliance with the statute on the part of ministerial officers with respect to such fees and allowances as are prescribed by law, they cannot refuse to be bound by its limitations in matters that are left to their discretion. That discretion must be in accordance with, and not in conflict with, the policy of the law."

§ 2050. "Retainer Fees," No Place in Bankruptcy.—"Retainer fees" have no place in the allowance of attorneys' fees out of bankrupt estates.²⁷ "Contingent fees" are reprehensible.²⁸

§ 2051. Mere Incidental Benefit from Services in Opposing Adjudication, etc., Not Sufficient.—Mere incidental benefit, such, for in-

²⁷. As to involuntary bankrupts, see *In re Mayer*, 4 A. B. R. 241, 101 Fed. 694 (D. C. Wis.). But compare facts, *In re Byerly*, 12 A. B. R. 187, 128 Fed. 637 (D. C. Pa.). And compare, *In re*

Smith, 5 A. B. R. 564, 108 Fed. 39 (D. C. N. Car.).

²⁸. *In re Young*, 16 A. B. R. 108, 142 Fed. 891 (D. C. N. Car.).

stance, as the causing of an amendment to the petition in a vital point by demurring thereto, is not to be a subject of compensation out of the estate, of attorneys resisting the petition.

Frank v. Dickey, 15 A. B. R. 155, 158, 139 Fed. 744 (C. C. A. Mo.): "In litigation, counsel often receive valuable suggestions from opposing counsel, which, as in this case, were not intended, when given, to be helpful; and they do not because of such suggestions, feel bound to share their fees with such opposing counsel."

Nor, for instance, where, in a contest over the election of a trustee, claims are successfully disputed by a creditor.^{28a}

§ 2052. Showing to Be Made of Propriety and Reasonableness.—Showing should be made affirmatively of the propriety and reasonableness of the allowance asked for.²⁹

In re Lane Lumber Co., 30 A. B. R. 749, 206 Fed. 780 (D. C. Idaho): "Was a service performed? Was such service reasonably necessary to enable the bankrupt to discharge its duties under the law? And what was it reasonably worth? The burden is upon the claimants to make a prima facie showing upon each of these three heads."

And it is the duty of the court to scrutinize the fee bills carefully, whether any party is appearing to object thereto or not.

§ 2052½. Mere Employment and Service Not Sufficient.—Merely that an attorney has been employed and services been rendered by him is not sufficient to warrant a charge therefor out of the estate. Showing of necessity or propriety and reasonableness is requisite.

In re (T. E.) Hill Co., 20 A. B. R. 73, 159 Fed. 73 (C. C. A. Ills.): "Ordinarily, the duties of this statutory receiver neither require nor justify employment of an attorney, and it is plain that no claim for such services is chargeable per se against the estate, predicated alone upon the fact of employment and service rendered. The court may well reject claims therefor, as 'not a proper charge on said trust estate' (in the terms of the present order), in the exercise of a sound discretion to limit expenditures of administration within just bounds, and various considerations may enter into the disapproval."

§ 2053. Notice to Creditors Not Requisite, unless by Local Rule.—No notice is required to be given creditors of applications for allowance of attorney's fees out of bankrupt estates, unless by special rule of court.³⁰

In re Stotts, 1 A. B. R. 641, 93 Fed. 438 (D. C. Iowa): "The question remains whether notice to the creditors was a prerequisite to this allowance by

^{28a}. See ante, § 2018.

²⁹. Inferentially, In re Lewin, 4 A. B. R. 632, 103 Fed. 850 (D. C. Vt.); impliedly, In re Rosenthal & Lehman, 9 A. B. R. 626, 120 Fed. 848 (D. C. Mo.); perhaps, In re Woodard, 2 A. B.

R. 694, 95 Fed. 956 (D. C. N. Car.); Ohio Valley Bank Co. v. Mack, 20 A. B. R. 919, 163 Fed. 155 (D. C. Ohio).

³⁰. In re [K. L.] Wong, 30 A. B. R. 125 (D. C. Hawaii).

the referee. The section of the statutes (§ 64, par. b) as to the debts having priority of payment does not expressly require notice to the creditors before costs of administration can be determined and allowed. In the section (§ 58, par. a) which states in what matters notice to creditors must be given, no requirement appears for such notice when costs of administration are to be settled and allowed; and my attention has not been directed to any other provision of the statute, nor of the general rules, making such notices obligatory to the setting of such costs. Is there any good reason otherwise requiring such notice? It is assumed that creditors whose claims are filed with the referee will inform themselves of the general proceedings in the estate sufficiently, at least, to advise them of its general status, and file their objections, and, if necessary, take the proper steps for review of whatever orders and proceedings they may wish reviewed. They are thus given abundant opportunity for guarding against improper allowances. If the referee shall deem it proper, whether because of the peculiarity of the claim for costs or expenses, or for any other reason by him deemed sufficient, I see no objection to his fixing a time for the hearing and notifying the creditors that at that time he will pass on the claim. But there occurs to me no good reason why the costs and expenses of administration must be passed upon by a creditors' meeting, before he shall pass on the same. If at any time before the closing of the estate this court shall find that excessive attorney's fees have been allowed and paid, this court doubtless has the power to take whatever steps are found necessary to correct this improper allowance and payment. These attorneys are on the roll of this court and subject to any proper order this court may make.

"I am of the opinion that notice to creditors is not required before the referee can settle proper attorney's fees."

However, it is a wise check upon extravagant applications and allowances to require such notices to be given, and such is the local rule of court in some districts.³¹

§ 2053½. Application for Allowance Not Properly in Attorney's Own Name.—The application for allowance of attorney's fees properly should be made in the name of the petitioning creditors, receiver, trustee or bankrupt, respectively, and not in the attorney's own name, for the attorney has no independent standing—his rights are derived through the parties or officers who employ him.³²

§ 2054. Trustee's and Receiver's Attorney's Fees.—Although not expressly provided for by the statute, as are attorney's fees for petition-

³¹. Instance, *In re Young*, 16 A. B. R. 109, 142 Fed. 891 (D. C. N. C.).

³². [Petitioning creditors] *In re Young*, 16 A. B. R. 108, 142 Fed. 891 (D. C. N. Car.).

[At any rate so far as the bankrupt's attorney is concerned] *In re Lane Lumber Co.*, 30 A. B. R. 749, 206 Fed. 780 (D. C. Idaho). Also compare post, § 2054, notes.

But compare, where objection was made that the trustee's accounts were

silent upon the subject of attorney's compensation and that the attorneys presented their claims direct and on their own behalf. *In re Smith*, 29 A. B. R. 628, 203 Fed. 369 (C. C. A. Mich.): "In the light of the judges finding of fact that it has been general practice (though without any rule on the subject) to allow the attorneys to file papers in their own name, 'on claim for services rendered' the objections grouped under subdivision (c) are not well taken."

ing creditors and bankrupts, yet attorney's fees are allowable in proper cases as part of the trustee's expenses.³³

In *re Byerly*, 12 A. B. R. 186, 128 Fed. 637 (D. C. Penn.): "There is no direct provision in the Bankrupt Act for the payment of the fees of attorneys employed by the trustee, but they come in as part of the administration of the estate like other necessary expenses."

Page *v. Rogers*, 17 A. B. R. 854, 149 Fed. 194 (C. C. A. Tenn.): "The reasonable fees of counsel employed by the trustee to recover a voidable or fraudulent preference made by the bankrupt constitutes a part of the trustee's expenses, and as such a part of the costs and expenses of administration entitled to preferential payment. * * * These counsel fees were therefore a part of the trustee's expenses and allowable under our mandate."

Indeed, part of the usual and ordinary expenses of the receiver and trustee are attorney's fees. There are almost always legal questions arising in the course of the administration that require the advice and action of an attorney; and attorney's fees are frequently quite as necessary a part of the expenses as are the wages of the watchman, guarding the property from robbery and fire.³⁴

In *re McKenna*, 15 A. B. R. 6, 137 Fed. 611 (D. C. N. Y.): "It was his duty to look out for and protect the interests of the creditors, and in view of the fact that the bankrupt, with upwards of \$20,000, which came to and vested in him the same day he filed his petition in bankruptcy, and before he was adjudicated a bankrupt, took the position that the creditors were entitled to no part of it, and that under the Bankrupt Act he was entitled to a discharge from all his debts, while retaining the whole legacy, the trustee would have been culpably remiss in the discharge of his duty, had he not employed counsel, and good counsel, in the matter, and it was his duty to have such counsel present at all the hearings before the surrogate and in both proceedings."

In *re Erie Lumber Co.*, 17 A. B. R. 702, 150 Fed. 817 (D. C. Ga.): "This reasoning was adopted in *In re Burke*, 6 A. B. R. 502, where it is declared that 'legal services are often quite as actual and necessary as are doors and locks and roofs.'"

In *re Abram*, 4 A. B. R. 575, 103 Fed. 272 (D. C. Calif.): "The trustee of an estate in bankruptcy is entitled to the advice and assistance of counsel when necessary for the proper discharge of his duties as such trustee, and the reasonable expense incurred by him for such a purpose may be allowed as a charge against the estate; but the court will not, ordinarily, in the first instance, undertake to give any direction to the trustee in the matter of the employment of an attorney. The trustee must exercise a reasonable judgment in that matter; that is, he must exercise a reasonable judgment as

33. In *re Stotts*, 1 A. B. R. 641, 93 Fed. 438 (D. C. Iowa); In *re Rozinsky*, 3 A. B. R. 830, 101 Fed. 229 (D. C. N. Y.); In *re Hitchcock*, 17 A. B. R. 664 (D. C. Hawaii); In *re Mitchell*, 1 A. B. R. 688 (Ref. Pa.); *Davidson v. Friedman*, 15 A. B. R. 490, 140 Fed. 853 (C. C. A. Tenn.); In *re Burke*, 6 A. B. R. 502 (Ref. Ohio); (1867) In *re Noyses*, 6 B. Reg. 277 Fed. Cas. 10,371.

But, for a case holding that attorney's and stenographer's fees for con-

ducting a general examination of the bankrupt and witnesses for the benefit of general creditors should not be permitted to absorb the fund at the expense of workmen and other priority claimants, see In *re Rozinsky*, 3 A. B. R. 830, 101 Fed. 229 (D. C. N. Y.).

34. In *re Stotts*, 1 A. B. R. 641, 93 Fed. 438 (D. C. Iowa): This decision is not to be accepted as authority on the question of bankrupt's attorney's fees.

to the necessity for securing the assistance of counsel—such judgment as a man of ordinary prudence would use in the transaction of his own business. When professional services have been rendered by an attorney to the trustee in his official capacity, the court will, in a proper proceeding, determine whether the employment of such an attorney was necessary, and, if found necessary, the reasonable value of his services.”

Likewise the receiver is entitled in proper cases to employ counsel.³⁵

In *re Oppenheimer*, 17 A. B. R. 59 (D. C. Pa.): “A receiver in bankruptcy is undoubtedly entitled to the assistance of counsel, the same as an executor or administrator, and upon the same grounds; and a reasonable allowance therefor will be made him in the settlement of his accounts. They come in, however as part, of the expenses of administering the estate and not otherwise; and there is no place for anything outside of this.”

Ordinarily, however, the duties of the receiver, as a mere custodian, neither require nor justify the employment of an attorney; and certainly an attorney is not to be employed as a mere matter of course nor his services compensated for out of the estate merely because rendered.

In *re (T. E.) Hill & Co.*, 20 A. B. R. 73, 159 Fed. 73 (C. C. A. Ills.): “Ordinarily, the duties of the statutory receiver neither require nor justify employment of an attorney, and it is plain no claim for such services is chargeable per se against the estate predicated alone upon the fact of employment and service rendered.”

The receiver’s attorney will not be allowed compensation where his services were unnecessary and where the receivership itself was clearly unjustified.³⁶

And attorneys who have entered into an illegal and unprofessional agreement with the receiver, respecting their compensation, will not be allowed counsel fees from the estate, though their actual disbursements may be provided for.³⁷

The attorney for the trustee, but not an attorney for an assignee, seeking allowance, it has been held in one case, is entitled to be heard in behalf of his fees.³⁸

But the better rule undoubtedly is that he has no independent standing and must work out his rights through the trustee, like the other persons employed by the trustee. Undoubtedly, in cases where the trustee is insolvent and not responsible in damages, any employee who has been rendering assistance to the trustee may be heard in his own behalf, but this is because of the trustee’s individual lack of responsibility.³⁹

^{35.} In *re Erie Lumber Co.*, 17 A. B. R. 702, 150 Fed. 817 (D. C. Ga.). For instances, see ante, § 2045.

Not to Employ Bankrupt’s nor Petitioning Creditor’s Attorney.—But it has been held he should not employ either the bankrupt’s nor the petitioning creditor’s attorney. In *re Strobel*, 20 A. B. R. 22, 160 Fed. 916 (C. C. A. N. Y.).

^{36.} In *re Desrochers*, 25 A. B. R. 703, 183 Fed. 991 (D. C. N. Y.).

^{37.} In *re Oshwitz & Feldstein*, 25 A. B. R. 594, 183 Fed. 990 (D. C. N. Y.).

^{38.} In *re Byerly*, 12 A. B. R. 186, 128 Fed. 637 (D. C. Penn.).

^{39.} To same effect, In *re Young*, 16 A. B. R. 108, 142 Fed. 891 (D. C. N. Car.).

Where, however, the rules require the court to make a preliminary order authorizing the employment of the attorney, the attorney would seem to occupy a quasi-official position sufficient to warrant him to present his application for compensation in his own name; and such is the practice in some districts.⁴⁰ But in any event the attorney could hardly be permitted to prosecute appeal or error proceedings in his own name.⁴¹ The receiver is responsible for his attorney's acts.⁴²

No necessity exists for the trustee to pay his attorney first and then to seek reimbursement. He should get an order first, however, before paying his attorney from the estate's funds.⁴³

The receiver, it has been said, should engage only counsel that stand independent of the parties of the litigation.⁴⁴

In *re Smith*, 29 A. B. R. 628, 203 Fed. 369 (C. C. A. Mich.): "The general rule is that a receiver may not employ the solicitor of either of the parties to the suit in which he is appointed (Beach on Receivers, § 262); and this rule applies to trustees. But it is only when the receiver is acting adversely to one of the parties that there is any impropriety in his employing the counsel of the other (Beach on Receivers, § 263; High on Receivers, § 217; Alderson on Receivers, § 233). The general rule doubtless is that a trustee or a receiver should not ordinarily employ the attorney who represents the bankrupt or an attorney who represents interests in the litigation which are adverse to the general estate, or in conflict with other interests represented by the trustee; and where there are matters in controversy between different classes of creditors, the court will usually decline to authorize the employment by the trustee of an attorney representing one of such classes."

However, a rule prohibiting the employment of the petitioning creditors' attorney by the receiver or trustee is likely to weaken the vigor of bankruptcy proceedings, substituting, as such rule naturally would tend to do, any indifferent attorney for one who, though a partisan, yet in all likelihood has been first on the scene, at a time when the bankrupt's plans of defense had not yet been formulated and when the evidence was still fresh, and who for those reasons occupies an especially advantageous position for thwarting conspiracies and tracing and recovering concealed assets. If

40. For example, in the Southern and Eastern Districts of New York, compare, In *re Smith*, 29 A. B. R. 628, 203 Fed. 369 (C. C. A. Mich.).

41. But see *Gray v. Mercantile Co.*, 14 A. B. R. 780, 138 Fed. 344 (C. C. A. N. Dak.), where, when the trustee did appeal from an order cutting down his expenses and commissions the circuit court held he was, because he was the representative of creditors, opposed to his own claims—an absurdity, to be sure.

42. *Mason v. Wolkowich*, 17 A. B. R. 712, 721, 150 Fed. 699 (C. C. A. Mass.).

43. In *re McKenna*, 15 A. B. R. 6, 137 Fed. 611 (D. C. N. Y.).

44. In *re Kelly Dry Goods Co.*, 4 A.

B. R. 530, 102 Fed. 747 (D. C. Wis.).

Trustee Employing Bankrupt's Attorney, on Re-Opening of Estate, to Collect Old Judgment Obtained by Him Before Bankruptcy, No Attorney's Lien on Amount Collected for Services Performed before Bankruptcy.—Where the trustee, on a re-opening of the estate, employed the former bankrupt's attorney to collect an old judgment which the attorney had obtained before the bankruptcy, the attorney has been held not entitled to retain any portion of the amount collected to apply on his fees earned before the adjudication. In *re Blum*, 28 A. B. R. 60, 193 Fed. 304 (D. C. N. Y.).

there be danger of collusion between the petitioning creditors and the bankrupt, as frequently there is, it would seem unfortunate that such danger could not be directly provided against rather than by such a rule, at best an indirect preventive, and so likely to weaken the efficiency of the law.

The trustee must exercise reasonable judgment in employing counsel. It has been held that the court will not undertake to give any direction, but will pass upon the propriety of the employment and the reasonableness of the fee therefor, after the services have been rendered;⁴⁵ but, this cannot be laid down as a hard and fast rule, and, on the contrary, the rule in many districts requires a preliminary application on showing made to the court for leave to employ counsel.⁴⁶ Though the trustee should not, as a rule, employ the bankrupt's attorney as his own attorney, yet after services have been rendered by the bankrupt's attorney for him the attorney should not be refused compensation on that ground.⁴⁷

§ 2055. Not to Employ Attorney to Do Ordinary Business Duties of Trustee.—Trustees should not be allowed reimbursement of attorney's fees for doing those things which an ordinary business man is supposed to know how to do. Sometimes, indeed, attorney's bills are presented that provoke the query: What is it that the trustee himself did in this case—was he a mere figurehead?

Obiter, *Ohio Valley Bank Co. v. Mack*, 20 A. B. R. 919, 163 Fed. 155 (D. C. Ohio): "The trustee is a lawyer and an able one, and should not employ lawyers to do any work which the law requires him to do."

Thus, no allowance of attorney's fees should usually be made for selling property—that is one of the very duties of a business man which the trustee, presumably, is elected by creditors to perform.

In *re Mercantile Co.*, 2 A. B. R. 419, 95 Fed. 123 (D. C. Mo.): "It is further claimed by these attorneys, as a basis of their compensation, that they induced several bidders to attend the sale of the property of the bankrupt, 'and the property yielded in cash the sum of \$4,207.' Presumptively and naturally enough, interested creditors in the estate would either attend in person, or be represented at such sale, to see that the property be not sacrificed, as they are the especial beneficiaries in the product of the sale. No provision of the Bankrupt Act even squints at an allowance against the estate for such service."

* * *

"While the court personally would be pleased to exercise a spirit of large liberality both towards the attorneys and its officers assisting in the administration of bankrupt estates, it must be understood that the court is impressed with a sense of the obligation imposed upon it by the Bankrupt Act to so administer it as to preserve both the letter and the spirit of the statute, and produce the best results in behalf of creditors. Any other course taken by the courts in administering this statute will inevitably, as it has done in the past,

⁴⁵. In *re Abram*, 4 A. B. R. 575, 103 Fed. 272 (D. C. Calif.).

⁴⁶. Compare, inferentially, In *re*

Smith, 29 A. B. R. 628, 203 Fed. 369 (C. C. A. Mich.).

⁴⁷. In *re Dimm & Co.*, 17 A. B. R. 119, 146 Fed. 402 (D. C. Pa.).

invite additional legislation by Congress still further reducing the fees both of attorneys and of the officers of the court."

Mason v. Wolkowich, 17 A. B. R. 712, 150 Fed. 699 (D. C. Mass.): "No necessity whatever appears for the employment of counsel. Upon the facts shown the court would not have sanctioned any such employment, at least so far as the management of the sale was concerned. Employment of counsel to perform that part of the receiver's duties would certainly not have been approved by the court, and to perform them was no part of the proper duties of counsel, however employed. A sale made as this was, by persons never authorized to make it, could not have been upheld if its validity had been disputed at the time."

Frequently attorney's fees for procuring insurance are asked for. Of course, sometimes legal advice and legal opinions to the insurance companies may be necessary, but usually this is merely a business man's duty.⁴⁸

Compare, *In re Byerly*, 12 A. B. R. 186, 128 Fed. 637 (D. C. Penn.): "The estate was not a large one, the whole amount passing through the hands of the accountant in both his capacities not exceeding \$550, exclusive of the bankrupt's exemption; neither does it seem to have been seriously involved. It presented simply the ordinary case of a small commercial failure in which the services of counsel were only needed to a limited extent."

It is not proper in this relation to apply the same rule applicable to executors and administrators, nor even that applicable to assignees for the benefit of creditors. In the case of executors and administrators, and even of assignees, there is no presumption of any special fitness on the part of the incumbent nor of his experience in business affairs; the will of the decedent or assignor, or the statutes of the state, throw the administration in many cases into the hands of inexperienced persons, frequently women totally unacquainted with business affairs, who must of necessity employ some one more experienced to perform even the ordinary business duties of the office. Therefore, it may not be improper to allow attorney's fees for such services in the state courts. It is not so, however, in bankruptcy. The trustee is the choice of creditors and is presumed to have been elected because of his peculiar fitness to perform the duties of his office, and he certainly should be qualified to perform the ordinary business duties of the office.

§ 2056. Fees Allowable for Investigating and Resisting Improper Claims.—The trustee is entitled to reimbursement for attorneys' fees and expenses in investigating claims of creditors and resisting those he deems improper.⁴⁹

§ 2057. But Creditors Not So Entitled, Even for Successful Objections to Claims, before Election of Trustee.—But creditors are not

48. Compare, *In re Mercantile Co.*, 2 A. B. R. 419, 95 Fed. 123 (D. C. Mo.).

49. *In re Lewensohn*, 9 A. B. R. 368,

121 Fed. 1 (C. C. A. N. Y.). Obiter, *In re Fletcher*, 10 A. B. R. 398 (Ref. N. Y.).

entitled to attorney's fees nor to reimbursement for stenographer's fees paid by them in successfully objecting to claims of other creditors previously to the election of a trustee.⁵⁰

Inferentially, *In re Mercantile Co.*, 2 A. B. R. 419, 95 Fed. 123 (D. C. Mo.): "The court finds no warrant in any provision of the Act for compensating attorneys of petitioning creditors for their service in attending meetings of the creditors, and resisting the allowance thereof of other claims against the estate. They are supposed in such action to be subserving the interests of their client, whose dividend in the estate would be augmented in the proportion of the disallowance of other claims. Each creditor of the estate is interested in seeing meritless claims defeated and preferential claims rejected. And one of the objects of creditors' meetings is to afford each creditor an opportunity to object before the referee to the allowance of questionable claims, and each creditor has the right to object and make contest. Is the court to allow a fee to the attorney of each objecting and contesting creditor, when the statute expressly provides that 'one reasonable attorney's fee for professional services actually rendered, irrespective of the number of attorneys employed,' may be allowed by the court."

§ 2058. No Fees for Preparation of Papers Where Supreme Court's Forms Adequate.—Trustees should not be allowed for attorney's fees in doing these things for which the Supreme Court has already provided forms, unless the circumstances are exceptional and the forms inadequate. Thus, a trustee sometimes asks allowance for attorneys' fees for legal services in applying for the appointment of appraisers and drawing the journal entry for the same. All the trustee ought to do is to call upon the referee and mention his desires and get the blank that is supplied on demand. So with trustee's reports, although, of course, sometimes trustee's reports require legal assistance in their preparation. Perhaps it is permissible to allow for legal advice as to whether such forms exist and are applicable.

§ 2059. Whether Trustee Allowed Attorney's Fees for Own Professional Services.—It has been held that a trustee who is also an attorney at law may not be allowed attorney's fees for his own legal services to the estate, even where such services are necessary.⁵¹

In re Halbert, 13 A. B. R. 399, 134 Fed. 236 (C. C. A. N. Y.): "In support of the order sought to be reviewed, reference is made to two decisions: *In re Mitchell*, 1 Am. B. R. 687, and *In re Welge* (D. C.), 1 Fed. 216. Both of these were under the Bankruptcy Act of 1867, which provides that: 'In addition to all expenses necessarily incurred by him in the execution of his trust in any

⁵⁰. See ante, § 2018, and post, § 2071. *In re Fletcher*, 10 A. B. R. 398 (Ref. N. Y.); *In re Medina Quarry Co.*, 27 A. B. R. 466, 191 Fed. 815 (C. C. A. N. Y.).

Perhaps, *In re Coventry Evans Furn. Co.*, 22 A. B. R. 623, 166 Fed. 516, 171 Fed. 673 (D. C. N. Y.).

⁵¹. *In re Felson*, 15 A. B. R. 185, 139 Fed. 281 (D. C. N. Y.); *In re McKenna*, 15 A. B. R. 4, 137 Fed. 611 (D. C. N. Y.); compare, *In re Evans*, 8 A. B. R. 730, 116 Fed. 909 (D. C. N. Car.); contra, *In re Mitchell*, 1 A. B. R. 687 (Ref. Pa., disapproved in *In re Felson*, 15 A. B. R. 185, 139 Fed. 281, D. C. N. Y.).

case, the assignee shall be entitled to an allowance for his services in such case on all moneys received and paid out by him thus: [Giving various percentages].’ It must be assumed that Congress was advised of the fact that, under the language above cited, there had been occasions when trustees in bankruptcy who happened to be lawyers were allowed compensation for legal services in addition to their commissions, contrary to the almost universal practice, which refuses such allowances in the case of executors or of trustees generally. Presumably, it was to provide against such allowances being made under the Bankrupt Act of July 1, 1898, that Congress, in section 48 of such Act, provided as follows: ‘Trustees shall receive in full compensation for their services, payable after they are rendered [the various percentages therein state].’ This language is so precise, so unambiguous, and so explicit as to preclude the allowance of additional compensation upon any theory of a dual personality.

“The order of the District Court is reversed, and the claim for extra services is disallowed.”

While this rule seems unnecessarily strict yet it is established by the overwhelming weight of authority relative to the subject of trustees and attorney fees in other branches of law, as well as here; the rule arising from the difficulty of dissevering the interests of the employer and the employed where the trustee employs himself as attorney. However, on principle there would seem no good reason for prohibiting such allowance altogether. Certainly, the trustee’s intimate acquaintance with the affairs of the estate would especially fit him to approach the legal questions involved with better appreciation than a stranger. Undoubtedly the services he has charged for should be scrutinized with particular care to the end that he may not be obtaining extra compensation for the performance of the trustee’s duties, under the guise of allowances for professional services, contrary to the prohibition of § 72 of the act. Yet on principle it would seem that careful scrutiny should not be converted into an absolute prohibition altogether under any and all circumstances.⁵²

52. No charge (it is held in one case) should be made against the estate for services rendered to the receiver by an attorney who represents any of the parties to the litigation, so long as he continues to occupy that relation: the receiver’s attorney should stand independent.

In *re Kelly Dry Goods Co.*, 4 A. B. R. 530, 102 Fed. 747 (D. C. Wis.): “It is the well-recognized rule in equity that the receiver shall engage counsel who stands independent of the parties to the litigation (Beach, Rec., § 262), and the estate is not chargeable for services which may be given to the receiver by the attorney for either party during the continuance of such relation. So, in the case at bar, unless the service for which the charge was allowed was both necessary and independent in the sense of the rule referred to, it is not allowable as an expense of the receivership. The purpose of the ap-

pointment of a receiver in bankruptcy is one of mere temporary custody, and the duties are generally of the utmost simplicity. If complications arise in which the parties before the court have opposing interests, he should not take counsel of either; and, if under any circumstances the attorney of either party is engaged by him, there must at least be complete severance of all service and duty to the litigant party. Otherwise, any service rendered must be deemed either gratuitous or in the interest of the original client. Here the attorneys for whom the charge is made appear both of record and in fact for the petitioning creditors before and after the receivership, are on the petition for adjudication of bankruptcy, on the application for a receiver, and subsequently appear for the creditors at the meetings held during the continuance and after the close of the receivership. Under such conditions, any

§ 2060. Attorneys for Creditors Co-Operating with Trustee's or Receiver's Attorney Not Entitled.—Where the trustee or receiver has an attorney, no compensation is allowable out of the estate to attorneys for creditors assisting him or co-operating with him, even though the services be valuable.⁵³

In *re Roadarmour*, 24 A. B. R. 49, 177 Fed. 379 (C. C. A. Ohio): "No authorities are cited in support of a proposition that an attorney employed by creditors to oppose claims, after the appointment of a trustee, may be allowed compensation for such services, unless in a case where the trustee has improperly refused to make defense. Such a rule would open the door to a confused and disorderly practice, entirely out of harmony with the theory of the Bankrupt Act. We do not wish to be understood as holding that creditors may not be permitted, under proper safeguards, to defend against the allowance of claims where the trustee refuses to make defense, or that the bankruptcy court has no authority in such case, under its general equity powers, to allow compensation to attorneys employed by creditors for the purpose of such defense—as was permitted in *re Little River Lumber Co.*, 3 Am. B. R. 682, 101 Fed. 558. It is enough to say that such a case is not before us."

In *re Felson*, 15 A. B. R. 185, 139 Fed. 275 (D. C. N. Y.): "Let the dividends go to the creditors, and let the creditors pay their attorneys. It is not for the court or referee to undertake, by 'allowances,' to see that the attorneys for creditors are taken care of. It is the duty of the court to take care of the creditors, and the duty of the creditors to take care of their attorneys, except in cases where allowances are directly authorized and permitted. The Bankruptcy Act of 1898 was framed and must be administered in the interest of creditors. This is a case where the transactions and conduct of the bankrupt justly aroused the indignation of the whole jewelry trade. The association took up the matter, and have pressed it honestly and sincerely in aid of the trustee; but this court cannot find, and indeed there has been no suggestion, that the trustee failed in his duty, so as to warrant allowances from the estate to creditors and associations who generously came to his aid because of the general desire and determination to vindicate the law."

Compare, In *re Fidler & Son*, 23 A. B. R. 16, 172 Fed. 635 (D. C. Pa.), wherein it was held that where a trustee had been derelict to his duty to such an extent that he had subsequently resigned to escape removal, an attorney for creditors who had stepped in and recovered assets and had become attorney for the new trustee was entitled to compensation from the estate from the time he took steps to have the former trustee removed. So far as this point is concerned, creditors might have been entitled to reimbursement for their attorney's fees and expenses from even an earlier period, under the provision of Bankr. Act, § 64 (b) (2). See ante, § 2016.

Similarly, the bankrupt's attorney should not be allowed for services properly performable by the receiver's or trustee's attorney, where a re-

service rendered must be referable to their engagement for their clients, and, if chargeable to the estate for any amount, are in that relation only and upon special order of the court. The objection to the allowance must therefore be sustained. So ordered."

⁵³. Probably, In *re Coventry Evans Furn. Co.*, 22 A. B. R. 623, 166 Fed. 516, 171 Fed. 673 (D. C. N. Y.); In *re Medina Quarry Co.*, 25 A. B. R. 405, 182 Fed. 508 (D. C. N. Y., reversing on other points, 27 A. B. R. 466, 191 Fed. 815, C. C. A. N. Y.). Also see post, § 2068.

ceiver or trustee has been appointed.⁵⁴

§ 2060½. Costs Out of Estate for Trustee's Successful Opposition to Bankrupt's Discharge.—The intent of the Amendment of 1910 to Bankruptcy Act § 14b, permitting the trustee to oppose the discharge of the bankrupt when authorized so to do at a meeting of creditors called for that purpose undoubtedly was to give opportunity for a discharge to be opposed at the expense of all creditors rather than that the expense thereof should be saddled upon one or more creditors.

See report No. 691 of the Senate Judiciary Committee, 61st Congress, 2nd Commission: "Thereby the expenses of the proceedings in opposition to discharge will be spread over all the creditors and not be borne by a single creditor who might file objections."

However, it is essential in order that the opposition to the bankrupt's discharge, even though successful, be at the expense of the estate, that it be made by the trustee himself and that the trustee shall have been duly authorized to make the opposition, at a meeting of creditors called for that purpose. So the successful opposition to the bankrupt's discharge by certain creditors cannot be charged against the estate so long as it was neither made by the trustee nor in his name nor authorized at a meeting of creditors called for that purpose.

(Though it does not appear whether this case was decided before or after the amendment of 1910) *In re Kyte*, 26 A. B. R. 507, 189 Fed. 531 (D. C. Pa.): "The matter in dispute in this case was certified to the court, on petition of certain creditors of the bankrupt, for review of the order of the referee, refusing to allow a bill of costs incurred by the petitioners and others, creditors of the bankrupt, in opposing the bankrupt's discharge, in which they were successful."
* * *

"The costs for which payment is herein authorized are such as are allowed by this act arising from the bankruptcy proceedings in the administration of the estate. The costs claimed are not directed to be paid by the act and they did not grow out of the administration of the bankrupt's estates. * * * All acts necessary to be done to accomplish the purpose of converting the assets of the estate and distributing the same to and amongst the creditors legally entitled thereto, as well as any act tending to increase the value of the estate, or in some material manner benefit the estate of the bankrupt, whereby the general interests of all the creditors may be advanced, constitute the administration of the estate. The intent of the law is to administer the estate for the general interests of all the creditors with the least possible expense, and to this end when any proposition of interest, as well as detrimental to the creditors is made, the law provides that all the creditors shall have notice of a time and place to meet and either assent to or disapprove of such proposition. This undoubtedly is a provision of the law which has been created to throw a safeguard around the interests of the creditors so that the opportunity for abuse or mismanagement of their interests may be reduced to a minimum.

"The payment of costs and expenses incurred in a collateral proceeding by a creditor or creditors, without the formal approval of the general creditors,

54. *In re Lane Lumber Co.*, 30 A. B. R. 749, 206 Fed. 780 (D. C. Idaho).

especially when it is not intended by such proceeding to increase the proceeds of the estate, should not be looked upon with favor. Such proceeding is administrative only when it tends to increase the income of the estate or prevent the waste of the estate in hand. In the present case it is not pretended that either of these ends were obtained, but on the contrary, it was a collateral proceeding instituted by certain of the bankrupt's creditors without the formal assent of the other creditors and without any apparent resultant benefit, either present or future, to any one; a personal action upon the initiative of those undertaking it, not administrative in character, and a personal triumph. The discharge of the bankrupt is a personal right and affects only personal rights and obligations, and the bankrupt is entitled to such discharge provided he has done nothing forbidden nor left undone anything required, whereby he may have forfeited such right to a discharge, but it does not affect the administration of his estate. The estate will be administered in the same manner whether or not the bankrupt is discharged, and the administration will be ended when all the dividends are disbursed and the estate is closed. This may occur before or after the question of the bankrupt's discharge has been finally determined; the administration of the estate will neither be retarded nor hastened on account of the discharge; they both proceed in regular course and in different channels. The costs in question not being costs fairly arising from the proceedings in the administration of the estate, it follows that the court is without warrant or justification to order the same to be paid out of the estate.

"It also seems that a contrary interpretation of the law would be a dangerous doctrine to establish, as instead of the true intent of the law being carried out, the bankrupt might be submitted to the danger of vexatious opposition, contents multiplied, and estates diminished for no higher reason than to satisfy the whims or prejudices of some individual creditor, or to create fees for ambitious counsel. It would certainly not tend to the economical administration of the estate."

§ 2061. Exhausting Entire Estate in Attorney's Fees in Efforts to Discover Assets.—The expense of general administration, including reasonable attorney's and stenographer's fees for conducting an examination, are chargeable against the estate even if they absorb funds that would have been sufficient, at any rate, to pay priority claimants. The priority claimants are not like secured creditors, the owners of specific property holding defeasible title, but are simply entitled to be paid first after the expenses necessary to a due administration of the estate have been taken care of, including such expenses as are proper in the discovery of assets.⁵⁵

§ 2062. Fee Bills, Properly, Should Be Itemized.—The attorney's fee bill must be itemized—each item of work done should be set forth in detail, with the date and value—and "lump sums" should not be allowed.⁵⁶

§ 2063. Petitioning Creditors' Attorney's Fees.—Petitioning creditors in involuntary cases are entitled to an allowance out of the estate, of one reasonable attorney's fee for professional services actually rendered.⁵⁷

^{55.} *Contra*, In re Rozinsky, 3 A. B. R. 830, 101 Fed. 229 (D. C. N. Y.).

^{56.} In re Knight, see note to In re Smith, 5 A. B. R. 560.

^{57.} Bankr. Act, § 64 (b) (3); In re Falkenberg, 30 A. B. R. 718, 206 Fed. 835 (D. C. N. Mex.). As to what are "reasonable" fees, compare § 2045.

§ 2064. **Is Matter of Right.**—Petitioning creditors are entitled to their reasonable attorney's fee as of right.⁵⁸

In *re Curtis*, 4 A. B. R. 17, 100 Fed. 784 (C. C. A. Ills.): "The attorney for the petitioning creditors is entitled to this reasonable fee as of right. Its allowance or disallowance is not a matter of discretion."

And the right is that of the petitioning creditors themselves and the attorneys have no independent standing but must seek their compensation through the petitioning creditors.⁵⁹

§ 2065. **Only One Fee, Irrespective of Number of Attorneys.**—Only one fee may be allowed, irrespective of the number of attorneys employed.⁶⁰

In *re Coney Island Lumber Co.*, 29 A. B. R. 91, 199 Fed. 197 (D. C. N. Y.): "If more than one attorney or set of attorneys render these services, there shall be a division of the fee, rather than duplication or multiplication. Hence, if one set of attorneys act for the petitioning creditors and are succeeded by others, or if the court sees fit or deems it necessary to allow some of the services on behalf of the petitioning creditors to be rendered by other attorneys, this will result in a division of the allowance, and not increase its amount. The provisions of the law must be complied with and the estate protected, and the statute is clearly broad enough to justify the court in protecting the estate, and in not allowing maladministration, through willful neglect, or through unintentional failure on the part of one set of attorneys to do what is necessary."

"The services to petitioning creditors are prior in time to the election of a trustee. They are for the benefit of the estate, in the same way in which the services of the trustee and his attorneys are for the benefit of the creditors generally; and no attorney should be allowed to receive compensation for work not done by him, but by some one else in his place, under a too strict interpretation of the statute; nor should the amount of the allowance be increased to satisfy all the parties at the expense of the estate."

Thus, where an involuntary partnership petition was filed, and afterwards the individual petition of one of the partners was also filed, and the two proceedings were consolidated, and allowances was made to the attorneys of the other partner for filing schedules, a later application by the voluntary bankrupt for attorney's services in procuring consolidation of the two proceedings will be refused.⁶¹

The term "one reasonable attorney's fee irrespective of the number of attorneys employed" is meant obviously to exclude compensation to different attorneys for traversing the same ground in preparation for trial and for more than what would be reasonable if one attorney alone conducted the trial. In so far as the compensation does not involve duplication of

58. *Smith v. Cooper*, 9 A. B. R. 755, 120 Fed. 230 (C. C. A. Ga.); In *re Erie Lumber Co.*, 17 A. B. R. 700, 150 Fed. 817 (D. C. Ga.).

59. In *re Young*, 16 A. B. R. 108, 142

Fed. 891 (D. C. N. Car.). Compare, § 2053½.

60. Bankr. Act, § 64 (b) (3).

61. Analogously (bankrupt's attorney fee): In *re Eschwege & Cohn*, 8 A. B. R. 282 (Ref. N. Y.).

services, it would seem not improper for more than one attorney to be employed. The statute is not directed against the *employment* of more than one attorney, but against the allowance of more than one reasonable attorney fee. Thus, the investigation of facts and law and other preparation necessary to place the other attorney in the same position, should not be allowed for; and, in case more than one attorney participate in the trial on behalf of the petitioning creditors, no more should be allowed for all than if there had been but one.⁶²

§ 2066. Apportionment Where Intervening Creditors Assist.—

Allowance to intervening creditors, joining in the petition, may be made by apportioning the one fee allowable, where the services rendered were valuable to the estate.⁶³

Indeed, in one case,^{63a} the intervening creditors' attorneys alone were granted the fee, since the original petition was insufficient to warrant adjudication and other facts in the case made it equitable to so order.

§ 2067. Apportionment in Cases of Consolidation.—Upon the consolidation of two proceedings, the one attorney's fee should be equitably divided among the attorneys for the respective petitions.⁶⁴

§ 2068. For What Services Allowable to Petitioning Creditors.

—Petitioning creditors' attorneys' fees should be allowed only for the actual and necessary legal work in procuring the adjudication and in performing such duties as may thereafter devolve upon them beneficial to the estate.⁶⁵

In re Hart & Co. L't'd, 16 A. B. R. 725 (D. C. Hawaii): "The petitioners appeared for creditors of the bankrupt and during the course of the proceedings

62. As to practice when, after allowance of one fee to the attorney's for one partner, the other partner applies for a similar allowance, see In re Eschwege & Cohn, 8 A. B. R. 282 (Ref. N. Y.). It would seem the better practice for the court to ascertain first whether the partnership had employed counsel and to allow the fee solely to the partnership counsel; or, in case of dissension between the members, to settle first who shall be entitled to the fee on notice to all partners.

Compare, as to receiver's attorney, In re Falkenberg, 30 A. B. R. 718, 206 Fed. 835 (D. C. N. Mex.).

63. But compare, although not contra, Frank v. Dickey, 15 A. B. R. 155, 139 Fed. 744 (C. C. A. Mo.), in which case allowance was refused for filing a second petition, not acted on, although by demurring to the first petition the second petitioners caused amendment in a vital point. Also, compare, In re Fischer, 23 A. B. R. 427, 175 Fed. 531 (C. C. A. N. Y.).

63a. In re Southern Steel Co., 22 A. B. R. 476, 169 Fed. 702 (D. C. Ala.).

64. In re McCracken & McLead, 12 A. B. R. 95, 129 Fed. 621 (D. C. La.).

But compare, Frank v. Dickey, 15 A. B. R. 155, 139 Fed. 744 (C. C. A. Mo.), where an allowance to the attorneys for the second petition was refused; other facts appearing, however, in this case, that undoubtedly had bearing on their refusal.

Upon consolidation of two petitions before the adjudication and reference the referee is not authorized to pass upon the necessity of filing the second petition. In re McCracken & McLead, 12 A. B. R. 95, 129 Fed. 621 (D. C. La.).

65. Inferentially, In re Curtis, 4 A. B. R. 17, 100 Fed. 784 (C. C. A. Ills.); Frank v. Dickey, 15 A. B. R. 155, 139 Fed. 744 (C. C. A. Mo.). Instance, In re Medina Quarry Co., 27 A. B. R. 466, 191 Fed. 815 (C. C. A. N. Y.); impliedly In re [Francis Levy] Outfitting Co. L't'd, 29 A. B. R. 8 (D. C. Hawaii).

were ordered by the court, there being no contest by the bankrupt, to assist in the preparation of the schedules of the said estate.

"I find that they are entitled to fees for professional services in preparing petition for adjudication, attendance at court, return day and the day set for hearing, at which time adjudication was granted; also for advising in the matter of continuance of business pending adjudication, interview with creditors after proceedings begun, and attending first meeting of creditors for appointment of trustee and examination of bankrupt. They are also entitled to fees for assisting the bankrupt in the preparation of the schedules."

Thus, attorney's fees should not be allowed for filing a second petition in bankruptcy, which was ignored and never acted upon;⁶⁶ even though the second attorney, by demurring to the first petition, causes an amendment of the first petition in a vital point;⁶⁷ nor for arguing in opposition to a motion to quash growing out of an error of the clerk of court in fixing the return day, which error might by due diligence have been mitigated by the attorney's early effort;⁶⁸ nor for amendments to the petition necessitated by their own oversight;⁶⁹ nor for arguing a motion due to their neglect to file a replication.⁷⁰ Nor should attorney's fees be allowed to petitioning creditors for consultation and investigations before it was finally determined to institute bankruptcy proceedings. Such services are for the clients themselves to take care of and are not chargeable against the estate.⁷¹

And it has been held that, save as to the filing fee, an allowance to the attorney for petitioning creditors will be refused where they were in sympathy with the bankrupt, and rendered services in opposition to the interests of the estate.⁷²

§ 2069. Allowance Not to Be on Basis of Plaintiffs' in Creditors' Bills.—The allowance is not to be made on the basis of what would be a reasonable fee for the attorneys of the plaintiff in a creditors' bill.⁷³

In re *Mercantile Co.*, 2 A. B. R. 419, 95 Fed. 123 (D. C. Mo.): "This court discovered, after administering this act for a season, that it was to be plagued and perplexed with what it conceived to be demands enormous in their extent for attorney's fees, both in involuntary and voluntary cases. The impression among lawyers in this particular seems to be that the proceedings in involuntary cases should be likened to the practice in chancery, and that, where a creditor files a bill in equity to reach the assets of an insolvent debtor for the benefit of creditors generally, an allowance for the attorney of the petitioning creditors should not only be made a charge upon the general fund, but its extent should be the largest liberality of the chancellor."

66. *Frank v. Dickey*, 15 A. B. R. 155, 139 Fed. 744 (C. C. A. Mo.).

67. *Frank v. Dickey*, 15 A. B. R. 155, 139 Fed. 744 (C. C. A. Mo.). But compare, *In re Southern Steel Co.*, 22 A. B. R. 476, 169 Fed. 702 (D. C. Ala.).

68. *In re [Francis Levy] Outfitting Co.*, 29 A. B. R. 8 (D. C. Hawaii).

69. *In re [Francis Levy] Outfitting Co.*, 29 A. B. R. 8 (D. C. Hawaii).

70. *In re [Francis Levy] Outfitting Co.*, 29 A. B. R. 8 (D. C. Hawaii).

71. *In re Hart & Co., Ltd.*, 16 A. B. R. 725 (D. C. Hawaii).

72. *In re Medina Quarry Co.*, 25 A. B. R. 405, 182 Fed. 508 (D. C. N. Y., reversed on other points, 27 A. B. R. 466, 191 Fed. 815).

73. *In re Goldville Mfg. Co.*, 10 A. B. R. 554, 123 Fed. 579 (D. C. S. Car.).

§ 2070. "**Amount Involved," Not Entire Estate but Only Surplus over Valid Liens.**—And in considering the element of "amount involved," the allowance to petitioning creditors should be based on the amount realized for creditors over and above good and valid liens; for the adjudication is of no interest nor benefit to the lienholders—their liens are unaffected. It is only of benefit to general creditors, to create a fund for them; and the limits of that fund measure the "amount involved."⁷⁴

Nevertheless, if the petitioning creditors' attorney's fees were partly incurred in preserving the mortgaged property, such part might properly be assessed against the mortgaged property, in accordance with the usual rules relative to the priority of the expense of preserving a fund over the rights of lienholders therein.⁷⁵

§ 2071. **No Fees to Petitioning Creditors for Objecting to Claims at Election of Trustee.**—Petitioning creditors are not entitled to attorney's fees, nor to reimbursement of stenographer's fees, paid by them in successfully objecting to claims of other creditors previously to the election of a trustee.⁷⁶

§ 2072. **Nor for Examination of Bankrupt after Appointment of Trustee.**—After the appointment of a trustee, no allowance to the petitioning creditors may be made for an attorney or counsel at the examination of the bankrupt, inasmuch as such services are either for the trustee or for the creditors individually.⁷⁷

§ 2073. **But Allowable for Pursuing Property before Adjudication.**—Attorney's fees may be allowed to the petitioning creditors, however, for pursuing property before the adjudication.⁷⁸

§ 2074. **None for Services after Election of Trustee.**—No allowance should be made to the petitioning creditors for services after the election of trustee.⁷⁹

In re Felson, 15 A. B. R. 191, 139 Fed. 275 (D. C. N. Y.): "His compensa-

74. Apparently contra, In re Erie Lumber Co., 17 A. B. R. 700, 150 Fed. 817 (D. C. Ga.). Impliedly, In re [Francis Levy] Outfitting Co., 29 A. B. R. 8 (D. C. Hawaii).

75. See post, §§ 2075, 2084.

76. See ante, §§ 2018, 2057. In re Medina Quarry Co., 27 A. B. R. 466, 191 Fed. 815 (C. C. A. N. Y., reversing S. C., 25 A. B. R. 405, 182 Fed. 508), quoted at § 2018. In re Fletcher, 10 A. B. R. 398 (D. C. N. Y.); inferentially, In re Mercantile Co., 2 A. B. R. 419, 95 Fed. 123 (D. C. Mo.).

Compare, to same effect, In re Worth, 12 A. B. R. 572, 130 Fed. 927 (D. C. Iowa), quoted at § 2018.

77. In re Silverman & Schoor, 3 A. B. R. 227 (D. C. N. Y.). But compare, In re Hart & Co., 16 A. B. R. 725 (D. C. Hawaii).

78. In re Medina Quarry Co., 27 A. B. R. 466, 191 Fed. 815 (C. C. A. N. Y.). But see In re Evans, 8 A. B. R. 730, 116 Fed. 909 (D. C. N. Car.): But on rehearing it appears there was a misunderstanding of the facts originally.

79. In re Medina Quarry Co., 25 A. B. R. 405, 182 Fed. 508 (D. C. N. Y., reversed on other points, S. C., 27 A. B. R. 466, 191 Fed. 815, C. C. A. N. Y.).

tion, however, must be confined to services rendered prior to the appointment of the trustee. Up to that time the petitioning creditors are the moving parties in behalf of creditors. Thereafter the trustee represents these interests."

§ 2075. No Allowance in General Out of Mortgaged Property Sold.—In general, no allowance should be made to petitioning creditors out of a fund derived from the sale of mortgaged property. They are concerned with the adjudication and in the surplus of the assets that will be rendered available to them by virtue of the adjudication⁸⁰ and that surplus should be the fund for their reimbursement and the limitation of their rights thereto.

In *In re Gillaspie*, 27 A. B. R. 59, 190 Fed. 88 (D. C. W. Va.): "The whole theory upon which the bankruptcy law authorizes the allowance of fees to the attorneys for petitioning creditors is that such creditors are acting for the joint benefit of themselves and all other unsecured creditors who will, by reason of their efforts, share equally with them in the unincumbered assets of the bankrupt. It is right and just that for this reason the fund secured to common creditors should, as against such creditors equally participating in it, share the expense incurred in securing it. But it is to be borne in mind that involuntary proceedings in bankruptcy can only be brought by unsecured creditors, and the fund that they can reach is only that which may arise after either the payment of the existing liens or from the sale of the property subject to liens. It must, therefore, always be a subject of careful consideration on the part of unsecured creditors whether it will be worth their while to proceed against one whose property is heavily incumbered, for they must do so taking the risk that no surplus fund will arise from which they may realize anything with which to pay their debts or the compensation due their attorneys.

"They can have no interest ordinarily in the funds necessary to pay off the valid subsisting liens, and certainly they cannot ask a court to pay their attorneys out of the funds due such lienholders for instituting and prosecuting a suit not calculated to benefit them, but only to diminish and lessen such lienor's vested right. It is true that it may be presumed that, if a man is bankrupt with his property incumbered with liens, a suit will have to be brought by some lienholder to marshal the liens and have sale decreed to satisfy the same. Therefore courts of bankruptcy, upon broad, equitable grounds, where there is reason to believe that the property may sell for an excess over the existing liens thereon, but it turns out that it does not, may well charge the actual costs of the suit and expenses of sale against the fund realized by the lienholders, for such costs of suit and expenses of sale would have had ordinarily to be incurred on some proceeding by them in order to sell and dispose of the property. But such allowance cannot extend further than this, and certainly not to the extent of compensating attorneys who have instituted the suit for unsecured creditors who have realized nothing. This is apparent for the very simple reasons, first, that lienholders cannot in any proceeding in equity to enforce liens be allowed compensation, as against other lienholders, for their attorneys in the suit instituted by them to enforce such liens; second,

80. See corresponding rule as to bankrupt's attorney's fees, post, § 2084. In *re Goldville Mfg. Co.*, 10 A. B. R. 554, 118 Fed. 892 (D. C. S. Car.); analogously (bankrupt's attorney), *Liddon v. Smith*, 14 A. B. R. 204, 135

Fed. 43 (C. C. A. Fla.); inferentially, *In re Utt*, 5 A. B. R. 383, 105 Fed. 758 (C. C. A. Ills.); contra, *In re Erie Lumber Co.*, 17 A. B. R. 700, 150 Fed. 817 (D. C. Ga.); contra, *In re Meis*, 18 A. B. R. 104 (Ref. Ky.).

because, if such attorney's fees be allowed, then the junior lienholder's lien may be utterly and wholly consumed at the instance of unsecured creditors instituting the bankruptcy proceeding; and, third, because attorney's liens for fees attach only to such funds as may be secured by their effort to their clients, and those others who are in the same class with them as regards interest."

But, as said, ante, § 2070, whatever part, if any, of the petitioning creditors' attorneys' fees was incurred in preserving the mortgaged property may be properly charged against the mortgage fund.

§ 2076. Review of Allowance of Petitioning Creditor's Fees by Appeal.—The allowance of the petitioning creditor's attorney's fees by the district court is reviewable by appeal to the circuit court of appeals under § 25 (a) (3), as being the allowing or rejecting of a claim or demand against the estate in excess of \$500.⁸¹ It is also reviewable by petition to revise.⁸²

§ 2077. Bankrupt's Attorney's Fees.—The bankrupt, in involuntary cases, is entitled to the allowance of one reasonable attorney's fee, irrespective of the number of attorneys employed, for professional services actually rendered to him while performing the statutory duties of the bankrupt; and in voluntary cases he may be allowed such attorney's fees as may seem proper in the court's discretion.⁸³

In re Rosenthal & Lehman, 9 A. B. R. 627, 120 Fed. 848 (D. C. Mo.): "This is an involuntary case, and therefore one reasonable attorney's fee, such as the court may allow for professional services actually rendered to the bankrupt while performing the duties prescribed by the act, should be included in and paid out of the estate as a part of the costs of administration.

"By the provisions of § 7 of the act (U. S. Comp. St. 1901, p. 3425) it is made the duty of the bankrupt in all cases to attend the first meeting of creditors, if directed by the court so to do; and when there, and at such other times as the court may order, 'to submit to an examination concerning the conducting of his business, the cause of his bankruptcy, his dealings with his creditors and other persons, the amount, kind and whereabouts of his property, and in addition all matters which may affect the administration and settlement of his estate.' The same section imposes other duties upon the bankrupt, some of which (like preparing schedules of property and list of creditors) from their nature justify and require the aid of professional counsel; while others (like complying with specific orders of court, or informing the trustee of any attempt known to him of creditors or other persons to evade the provisions of the act), from their essential nature, do not require, and would not justify, the employment of professional counsel to aid the bankrupt in their performance. And there are still other duties of the bankrupt (like attending the hearing upon his application for discharge from his debts) which may or may not require the aid of professional counsel in their performance.

"From these observations, as well as from the language employed in § 64b

⁸¹. In re Curtis, 4 A. B. R. 17 (C. C. A. Ills.). See post, subject of "Appeal and Review."

⁸². Instance, In re Fischer, 23 A. B. R. 427, 175 Fed. 531 (C. C. A. N. Y.).

⁸³. Bankr. Act, § 64 (b) (3); In re Christianson, 23 A. B. R. 710, 175 Fed. 867 (D. C. N. C.); In re Duran Mercantile Co., 29 A. B. R. 450, 199 Fed. 961 (D. C. N. Mex.).

(U. S. Comp. St. 1901, p. 3447), it seems clear that Congress did not intend by the provisions of the last-mentioned section to lay down a fixed rule authorizing a bankrupt to employ, at the expense of the estate, counsel to defend him in the performance of every duty prescribed by the act. Only such a reasonable attorney's fee as the court may allow in each individual case, and only such professional aid as the nature, exigency, and difficulty of the duty to be performed in each individual case reasonably require, seem to have been within the contemplation of Congress, as shown by a consideration of all the provisions of both sections in question.

"The test laid down in some cases, and which was applied by the referee in this case, is that legal services in aid of the administration of the estate should be paid for out of the funds of the estate, while those for the personal benefit or protection of the bankrupt should not be so paid. This may or may not be a correct test, but the difficulty arises in determining what services are purely personal, as distinguished from those which are incidental to the administration of the estate under the Bankruptcy Act. The act of 1898, like its predecessors, has, broadly speaking, two fundamental purposes—one to relieve an honest debtor from the incubus of overwhelming debt, and restore him to the activities of business life; another is to make a just and equitable distribution of the bankrupt's estate among his creditors. The true administration of an estate in bankruptcy is concerned as much with securing a discharge to the debtor as with the distribution of his assets, and to that end it is frequently essential for the bankrupt to make a full showing with relation to his property and business methods. He is ordered to appear before the referee for an examination touching 'the conducting of his business, the cause of his bankruptcy, his dealings with his creditors and other persons, the amount, kind and whereabouts of his property, and in addition all matters which may affect the administration and settlement of his estate.' The scope of this examination may, and frequently does, involve inquiries relative to matters about which the bankrupt has made oath, and other matters which, by § 14b, preclude discharge. Obviously the personal benefit and protection of the bankrupt at such an examination is involved, and so, also, the accomplishment of one of the main purposes of the act—to secure the discharge of an honest debtor—is involved. Thus it appears that what is for the personal benefit and protection of the bankrupt may also be of commanding importance in the just and impartial administration of the bankruptcy law."

It is proper for the referee of his own motion to reduce the amount allowed to the attorney by the trustee in his report, if it appears to be too large.

In *re Ferreri*, 26 A. B. R. 658, 188 Fed. 675 (D. C. La.): "In this matter appeal has been taken from the ruling of the Referee, first, as to his action in reducing on his own motion the fee of the attorney of the bankrupt. * * *

"There can be no doubt that the referee has the right, and it is his duty, to reduce the amount allowed by the trustee as fees of the attorney for the bankrupt, if too much. The law provides for one reasonable attorney's fee, and the Referee is by long odds in the best position to determine what is reasonable in the premises."

§ 2078. In Involuntary Cases, Confined to Services Rendered While Bankrupt in Performance of Duties Prescribed by Law.—The bankrupt's attorney's fee out of the estate in involuntary cases is con-

fined to professional services in assisting the bankrupt to perform the duties imposed upon him in § 7 of the act⁸⁴ and elsewhere in the law.⁸⁵

In re Payne, 18 A. B. R. 193 (D. C. N. Y.): "Under this it would seem that the basis of compensation is not payment for all services which the bankrupt may request of his attorney, but for the services to the bankrupt, in involuntary cases, while performing the duties prescribed upon the bankrupt by the bankruptcy law. Most of the work covered by the application for this allowance was apparently work done at the request of the bankrupt, and not work required from the bankrupt's attorney by the provisions of the statute."

In re Mayor, 4 A. B. R. 241, 101 Fed. 695 (D. C. Wis.): "The test for compensation out of the estate is whether the service is rendered in the performance of the bankrupt's duty in aid of the estate and its administration, and not whether the bankrupt stands in need of the service of counsel for his personal benefit and protection in any of the proceedings."

§ 2079. Actual Benefit to Estate Not Test, However.—Actual benefit to the estate is not, however, essential. The attorney for the bankrupt is not hired by the estate. His fees are for services rendered primarily to the bankrupt but which are, in many instances, equally beneficial to creditors by putting the estate in the course of an equal distribution in bankruptcy.⁸⁶

In re Christianson, 23 A. B. R. 710, 175 Fed. 867 (D. C. N. C.): "The services are not confined to those which are beneficial to the estate, but embrace those which are reasonably necessary to enable the bankrupt to perform his duties under the act and secure the benefit of its provisions. It should not be forgotten that the Bankruptcy Act is for the benefit of the bankrupt as well as his creditors. It is no less concerned that he shall be discharged from the burden of his debts than that he shall turn over all his property except his exemptions for the benefit of his creditors."

§ 2080. Services Must Be Reasonably Necessary and Actually Rendered.—In the absence of proof that the employment of counsel in a given case is reasonably necessary and that the services were secured and actually rendered in good faith to promote the purposes of the Bankrupt

⁸⁴ *In re Lane Lumber Co.*, 30 A. B. R. 749, 206 Fed. 780 (D. C. Idaho).

⁸⁵ Bankr. Act, § 64 (b) (3); *In re Stratemeyer*, 14 A. B. R. 120 (D. C. Hawaii); *In re Goldville Mfg. Co.*, 10 A. B. R. 552, 123 Fed. 579 (D. C. S. C.); *In re Michel*, 1 A. B. R. 665, 95 Fed. 803 (D. C. Wis.); *In re Connell & Sons*, 9 A. B. R. 474, 120 Fed. 846 (D. C. Penna.); *In re Anderson*, 4 A. B. R. 640, 103 Fed. 854 (D. C. S. C.); *In re O'Hara*, 21 A. B. R. 508, 171 Fed. 290 (D. C. Pa.); *Musica v. Prentice*, 31 A. B. R. 687, 211 Fed. 326 (C. C. A. La.), affirming 30 A. B. R. 555; *In re [Francis Levy] Outfitting Co.*, 29 A. B. R. 8 (D. C. Hawaii); *In re Hammel*

and *Hofman*, 31 A. B. R. 672, 211 Fed. 238 (D. C. N. Y.).

An attorney who merely prepares the bankrupt's schedules has been held sufficiently compensated by an allowance of twenty-five dollars. *In re Fullick*, 28 A. B. R. 634, 201 Fed. 463 (D. C. Pa.).

But compare where referee allowed attorney's fees for unsuccessful opposition to adjudication of bankruptcy. *In re Perlhefter & Shatz*, 25 A. B. R. 586 (Ref. N. Y.).

⁸⁶ *In re Kross*, 3 A. B. R. 187, 96 Fed. 819 (D. C. N. Y.). But compare, *In re Covington*, 13 A. B. R. 150, 132 Fed. 884 (D. C. N. C.).

Act, a claim therefor must be disallowed.⁸⁷

§ 2081. Must Be Professional Legal Services, and Not Merely Clerical or Business.—Neither clerical work, such as that of posting the bankrupt's books, so that the information therein contained would be available in making up the schedules; nor the making of extra copies of the schedules, after the first one was made, may be charged for at professional rates.⁸⁸ Nor may purely business assistance be so charged for.

And the attorney must disclose his financial dealings with his client that the court may act intelligently.⁸⁹

§ 2082. Legal Assistance in Preparing Schedules, Examining Claims at First Meeting, etc., Proper.—Thus the bankrupt may have fees allowed to his attorney for helping him prepare his schedules, for helping him examine claims so as to be able to report to the creditors whether the claims are correct or not, etc., etc.; for these are necessary services rendered him while he is engaged in the performance of his statutory duties.⁹⁰

In *re Lane Lumber Co.*, 30 A. B. R. 749, 206 Fed. 780 (D. C. Idaho): "The next is an item of \$750 for the preparation of the schedules. This being a duty clearly imposed upon the bankrupt, we have but to consider the nature and extent of the legal services necessarily involved therein and the reasonable value thereof. Unquestionably a measure of professional knowledge and skill is required for the proper discharge of such a duty, and perhaps in almost every case some allowance upon this account may properly be made, but I had supposed that rarely, if ever, could the amount exceed \$100, and commonly a much smaller sum would be adequate.

"It, is, however, contended that the case is an unusual one, and assuming it to be such we shall consider it upon its own merits. It is to be borne in mind that the duty of preparing the schedules is primarily imposed upon the bankrupt. He may secure such clerical and legal assistance as are reasonably necessary, but he cannot at the expense of the estate employ attorneys and shift to them the entire burden and responsibility. The statute provides that the bankrupt shall 'prepare, make oath to, and file in court' the schedule, setting forth certain facts; and it was contemplated that he should at least furnish the requisite information, and that the assistance provided for him at the expense of the estate would extend only to the matter of putting the information into the prescribed legal form.

87. In *re Rosenthal & Lehman*, 9 A. B. R. 626, 120 Fed. 848 (D. C. Mo.); In *re Duran Mercantile Co.*, 29 A. B. R. 450, 199 Fed. 961 (D. C. N. Mex.).

88. In *re Connell & Sons*, 9 A. B. R. 474, 120 Fed. 846 (D. C. Penn.); In *re [K. L.] Wong*, 30 A. B. R. 125 (D. C. Hawaii).

89. In *re Carr*, 9 A. B. R. 58, 117 Fed. 572 (D. C. N. Car.); In *re Smith*, 5 A. B. R. 563, 108 Fed. 39 (D. C. N. Car.).

90. In *re Kross*, 3 A. B. R. 187, 96 Fed. 816 (D. C. N. Y.); In *re Stratemeyer*, 14 A. B. R. 121 (D. C. Hawaii);

In *re Anderson*, 4 A. B. R. 645 (D. C. S. C.). Obiter, In *re Lewin*, 4 A. B. R. 632, 103 Fed. 884 (D. C. Vt.); (voluntary) In *re Hitchcock*, 17 A. B. R. 664 (D. C. Hawaii); In *re [K. L.] Wong*, 30 A. B. R. 125 (D. C. Hawaii); In *re Hammel and Hoffman*, 31 A. B. R. 672, 211 Fed. 238 (D. C. N. Y.); instance, In *re Fullick*, 28 A. B. R. 634, 201 Fed. 463 (D. C. Pa.), held \$25 sufficient for merely preparing brief schedules; In *re Duran Mercantile Co.*, 29 A. B. R. 450, 199 Fed. 961 (D. C. N. Mex.).

"It is not thought to be necessary to attempt a fine distinction between the duties which are strictly professional and those which are merely clerical, in the preparation of a schedule, but in estimating the compensation which should be allowed respect must be had to the nature of the work, for the compensation should be measured with regard to the character and quality of the service rather than the calling or profession of him by whom the service is rendered. Now it is not to be questioned that ordinarily the work of preparing a schedule is in the main that of an intelligent accountant. In *re Goldville Mfg. Co.* (D. C. S. Car.), 10 A. B. R. 552, 559, 123 Fed. 579, 586. With a few simple instructions touching the required contents of the schedule, the various headings under which assets and liabilities should be classified, and the formalities of execution, no competent accountant should experience serious difficulty in substantially complying with the law."

But it has been held that the bankrupt's attorney is not entitled to compensation for a mere attendance at the first meeting of creditors where his services were of no beneficial effect.⁹¹

In *re* [Francis Levy] Outfitting Co., Lt., 29 A. B. R. 8 (D. C. Hawaii): "Of these items the only one which could possibly be considered is that of 'attendance before referee at first meeting of creditors.' As to that item, there is no showing that the bankrupt's attorney rendered any services of value to the estate by his presence at the meeting; particularly, it does not appear that he there aided the bankrupt in any way in 'performing the duties * * * prescribed' by the statute. And it does appear from the referee's minutes in this matter that nothing was done at this meeting but the election of the trustee and the fixing of his bond, and that the meeting adjourned to a day certain for the important unfinished business of examining the president of the bankrupt corporation; at this meeting the bankrupt's attorney did not appear, nor on the day to which a further adjournment was had, when this examination finally took place. Had the attorney secured the preparation of the bankrupt's schedules of assets and liabilities, which have not yet been filed, and which the statute requires to be filed by an involuntary bankrupt 'within ten days, unless further time is granted, after the adjudication' (Bankruptcy Act, § 7), that would have been a work of some value to the estate, and assistance of this kind is noted as a good example of what the statute intended in allowing a fee to the bankrupt in 'performing the duties * * * prescribed' by law. All that could be allowed for attending the first meeting of creditors in a short session, such as here, and where the attorney was, so far as appears, of no assistance thereat, would be a nominal fee. But under the circumstances, where the attorney did not stay out the meeting through its adjourned session, at which important business was had, and has not, so far as appears, done anything to facilitate or encourage the performance of the bankrupt's first and most important duty (next to the physical discovery and delivery of assets) of filing his schedules, I do not feel justified in allowing any fee whatever. His diligence clearly entitles him to a fee, but he was serving his clients, the bankrupt and its officers, and to them alone must he look for his reward."

§ 2083. "Amount Involved" Not Entire Estate but Only Surplus over Valid Liens.—The value of the estate involved is to be considered in

⁹¹ Impliedly, In *re* Duran Mercantile Co., 29 A. B. R. 450, 199 Fed. 961 (D. C. N. Mex.).

the allowance of fees for the bankrupt's attorney.⁹² In estimating the element of "amount involved" in arriving at the reasonableness of the bankrupt's attorney fee, the amount of the entire estate is not to be taken but only the amount left outside of the valid liens,⁹³ as in cases of allowance to petitioning creditors for attorney's fees.

§ 2084. No Allowance Out of Mortgaged Property, Except for Mere Preservation.—No allowance should be made to the bankrupt's attorney out of the proceeds of mortgaged property, except where necessarily incurred in its mere preservation.⁹⁴

§ 2085. And None for Services in Opposing Bankruptcy Proceedings.—Bankrupt's attorney fees should not be allowed where they are incurred in opposing the progress of the bankruptcy proceedings rather than in assisting it.⁹⁵

Pratt v. Bothe, 12 A. B. R. 533, 130 Fed. 670 (C. C. A. Mich.): "By § 64b, the law provides for compensation to an attorney who assists the bankrupt in performing the duties imposed upon him. But this is done for the purpose of facilitating the proceedings, and for the benefit of the estate. It is not done in recognition of any contract obligation of the bankrupt. Many cases have been cited to us—mostly cases arising upon the last preceding act—in which the bankruptcy courts have given some countenance to the appellant's contention that the debtor may employ counsel to resist the petition of his creditors for an order adjudicating him a bankrupt, and charge his assets, with the payment thereof, and in one case that doctrine seems to have been quite pointedly held. In *re Comstock*, 6 Fed. Cas. 239, No. 3,074. The idea which pervades the allowance of such a charge seems to have been grounded upon a disposition to be merciful to the debtor, who, it is said, has given up all his property, and is without other means of repelling an unjust prosecution. But it is by no means a new thing—indeed, it is a situation constantly recurring—where a man, whether by his fault or his misfortune, is without means to make full defense of his property rights. It is unfortunate often, but it has never been thought that property belonging to others, or which might be adjudged to them, should be drawn upon to enable the man to make defense. Many cases are cited which more or less oppugn the doctrine of such decisions as *In re Comstock*, *supra*."

92. In *re Ellett Electric Co.*, 28 A. B. R. 453, 196 Fed. 400 (D. C. N. Y.). But that "amount involved" has no relevancy to bankrupt's attorney's fees, see *In re Lane Lumber Co.*, 30 A. B. R. 749, 206 Fed. 780 (D. C. Idaho).

93. See *ante*, § 2070. In *re Goldville Mfg. Co.*, 10 A. B. R. 552, 123 Fed. 579 (D. C. S. C.).

94. *Liddon & Bro. v. Smith*, 14 A. B. R. 204, 135 Fed. 43 (C. C. A. Fla.); analogously, *In re Goldville Mfg. Co.*, 10 A. B. R. 556, 118 Fed. 892 (D. C. S. C.). See *ante*, § 2075.

95. In *re Lewin*, 4 A. B. R. 632, 103 Fed. 850 (D. C. Vt.); In *re Anderson*, 4 A. B. R. 640, 103 Fed. 854 (D. C. S.

C.); In *re Felson*, 15 A. B. R. 185, 139 Fed. 275 (D. C. S. C.).

Inferentially, *Musica v. Prentice*, 31 A. B. R. 687, 211 Fed. 326 (C. C. A. La.), affirming 30 A. B. R. 555; In *re [Francis Levy] Outfitting Co. Lt.*, 29 A. B. R. 8 (D. C. Hawaii). But compare, *contra*, where bankrupt's attorney was allowed attorney's fees for unsuccessful opposition to the adjudication of bankruptcy. In *re Perlhefter & Shatz*, 25 A. B. R. 586 (Ref. N. Y.), one reason given therefor being that the same facts concerned the discharge. However, discharge also is not to be compensated for.

In *re Woodard*, 2 A. B. R. 692, 95 Fed. 955 (D. C. N. Car.): "There is no evidence before the court that the bankrupt has performed the duties prescribed. He made an assignment with preferences—the act of bankruptcy complained of—and has been actively engaged in trying to defeat or delay the proceedings at every stage, and making the proceedings as expensive as possible. To make the allowance for the services of an attorney in this behalf does not seem to be contemplated in the act. The court has seen and heard nothing to warrant the exercise of the discretion in this behalf."

Obiter, In *re Rosenthal & Lehman*, 9 A. B. R. 626, 120 Fed. 848 (D. C. Mo.): "It goes without saying that, if the services of counsel are secured, or, when secured, are employed for the purpose of screening the bankrupt from the consequences of his own wrongful conduct, or for the purpose of suppressing the truth, or otherwise thwarting the operation of the act, no compensation can reasonably be allowed by the court to be paid out of the assets of the estate. The test, in my opinion, is whether the employment is necessarily made, and the services necessarily rendered in good faith for the real purpose of so administering the act in a given case as to accomplish the purposes of its enactment. If the employment is reasonably necessary to aid either in the discovery of assets, or securing the bankrupt's discharge, or protecting the bankrupt from unjust charges or imputations or wrong, such as would subject him to the penalties of the act, a reasonable allowance should be made therefor. If, on the other hand, there is no reasonable necessity for the employment for either of the foregoing purposes, or if the employment is not in good faith to protect an innocent debtor in the assertion of his rights under the act, then no allowance should be made therefor."

Obiter, In *re Kross*, 3 A. B. R. 187, 96 Fed. 816 (D. C. N. Y.): "And the much more common 'service' in aiding the bankrupt to conceal, justify or extenuate questionable acts or transactions, must be equally excluded, since it is not 'reasonable' under § 60 or § 64 to charge the estate, to the detriment of creditors, for services in extricating or endeavoring to extricate or shield the bankrupt from difficulties caused by his own questionable conduct."

Whether, if the bankrupt is in contempt, his attorney's fees should be allowed him, the application therefor being in his own right, has not been decided, but it has been decided that if the application were made prior to the misconduct, the attorney's fees may be allowed, the attorney in no wise participating in the misconduct.

In *re Mayer*, 4 A. B. R. 239, 101 Fed. 695 (D. C. Wis.): "The bankrupt is in contempt, and clearly cannot move the court for any matter of indulgence until he has cleared his contempt. *Hovey v. Elliott*, 167 U. S. 409, 436, 17 Sup. Ct. 841, 42 L. Ed. 215. Whether this general rule would exclude him from invoking subsequently the benefits secured by statute of an allowance for his attorney is a question not presented on this record, for the reason that the application was made and the attorney's services were rendered before the occurrence of the contempt; and it is undoubted, both from the circumstances of the case and the reputation of his attorneys at this bar, that they were in no manner privy to the disobedience of the final order of the court. To the extent that such services were rendered within the intent of the statute, the subsequent misconduct of the bankrupt, without fault on the part of the attorneys, cannot serve to preclude the allowance of a fee."

Obiter, In *re Christianson*, 23 A. B. R. 710, 175 Fed. 867 (D. C. N. C.): "It cannot include services performed in an attempt to aid the bankrupt in

cheating his creditors, or evading any of the provisions of the act intended for their protection."

But where the attorney was not privy to the bankrupt's misconduct, he should not be denied a reasonable fee for services not aiding in the misconduct.⁹⁶

§ 2086. For Attendance at Bankrupt's Examination.—Bankrupt's attorney fees for attendance on the bankrupt's own examination are allowable. It has been contended that the bankrupt should not be entitled to reimbursement of his attorney's fees for the attorney's presence at the bankrupt's general examination, on the theory perhaps that all the bankrupt has to do on his general examination is to testify to the truth and that he needs no attorney to help him do that.⁹⁷ The practice, however, is the other way; and attorney's fees for attendance at the bankrupt's examination are customarily allowed.⁹⁸

In *re Duran Mercantile Co.*, 29 A. B. R. 450, 199 Fed. 961 (D. C. N. Mex.): "The next claim is for attending the bankrupt on several days before the referee. The court deems this attendance, if really for any great length of time, as largely unnecessary. There is nothing to show, either from the record or from the oral testimony, that there was any attack made upon the good faith of these bankrupts. Their presence before the referee was purely for the information of creditors. Presence of their counsel was hardly necessary, unless, perhaps, for the first day, because all they had to do was to tell what they knew about the business, and, if their failure was an honest one, no advice was necessary as to how to tell the truth. In this class of cases the court will consider, unless exceptional circumstances are shown, that an allowance of \$25 for assistance by the attorney to the bankrupt rendered before the referee is reasonable, and that will be allowed in this case."

In *re Lane Lumber Co.*, 30 A. B. R. 749, 206 Fed. 780 (D. C. Idaho): "The magnitude of the item, if not startling, at least challenges our attention, and gives sharp emphasis to the inquiry whether it is contemplated by the Bankruptcy Act that estates shall be burdened with the expense of furnishing a legal attendant for the bankrupt while he is present pursuant to an order of the court at the first meeting of creditors, and sessions of the court, either to give information or to submit to examination under oath. While contingencies doubtless may arise where the assistance of counsel may be reasonably required, it is thought that there is no presumption of such need, and that ordinarily attorney's fees for such services are not chargeable against the estate. * * * In the great majority of cases I can see no reason why the bankrupt should have the assistance of counsel in the performance of the simple duty

96. In *re Mayer*, 4 A. B. R. 238, 101 Fed. 695 (D. C. Wis.).

97. In *re Hammel and Hofman*, 31 A. B. R. 672, 211 Fed. 238 (D. C. N. Y.), wherein the court says that a bankrupt, in the ordinary case, does not need an attorney to attend at the hearing of his discharge or at the first meeting.

98. See ante, "Discovering Assets," §§ 1573, 1574. In *re Stratemeyer*, 14 A. B. R. 121 (D. C. Hawaii); In *re Mayer*,

4 A. B. R. 241, 101 Fed. 695 (D. C. Wis.); In *re Michel*, 1 A. B. R. 665, 95 Fed. 803 (D. C. Wis.); In *re Anderson*, 4 A. B. R. 645, 103 Fed. 854 (D. C. S. C.); In *re [K. L.] Wong*, 30 A. B. R. 125 (D. C. Hawaii).

Impliedly, In *re Adler & Co.*, 21 A. B. R. 302, 170 Fed. 634 (D. C. La.), wherein the court even refused to allow the bankrupt's attorney to be present.

required, or the burden of fees therefor imposed upon the estate. Quite obviously the purpose of requiring the attendance of the bankrupt is that he may give information, either voluntarily or under oath, touching any matter which may affect the administration and the settlement of the estate. He has no obligation except to disclose facts within his knowledge. He attends primarily as a witness, and there is ordinarily no more reason why he, as a witness, should have the protecting care of attendant counsel, than that any other witness under any other circumstances should have such protection. It is to be guarded against unwittingly or inadvertently doing or saying something which might be prejudicial to his right to a discharge in bankruptcy; if he is willing frankly to disclose the facts, he can, as a rule, suffer no prejudice. But here even that consideration is of little moment, for no one can be greatly concerned in the question whether or not a corporation shall be discharged, or in opposing such discharge. Nor could there here arise any question touching the matter of exemptions, for a corporation is not entitled to exemptions. Ordinarily, why should not the bankrupt put himself at the service of the trustee, who is presumably not antagonistic, and who should not, and presumably does not have any motive or incentive to injure him or prejudice him in any of his rights? Instead of laying the facts before counsel especially employed by him, why should he not disclose them directly to the trustee or the attorney for the trustee?

"If it were shown that the trustee and his attorney were disposed unjustly to attack him or to treat him unfairly, possibly he should have the assistance of counsel, but ordinarily it may be assumed that if any such disposition were shown the referee or judge would check it and see that his rights were protected while acting as a witness or informant, as the court will protect a witness against wrong or abuse in any other case or proceeding in which he appears in obedience to process."

Compare *In re Kross*, 3 A. B. R. 187, 96 Fed. 816 (D. C. N. Y.): "Ordinarily I cannot regard attendance by counsel for the bankrupt at all the various examinations as necessary. The restraints on discharge being confined to acts either criminal or most plainly fraudulent and wrong, the honest and straightforward debtor has rarely need of 'counsel,' unless falsely attacked, when professional aid may become proper and necessary, and should then be compensated. There is often, however, too much interference and objection by the bankrupt's attorney in the ordinary examination in behalf of creditors, which operates in every way injuriously. 'Services' of this kind should, of course, be ignored."

§ 2087. Whether Fees Allowable for Petition for Discharge, etc.

—It would seem, on reason, perhaps, that no attorney's fees should be allowed in involuntary cases for preparing the petition for discharge nor for defending the same, if it be attacked by creditors.⁹⁹

In re Duran Mercantile Co., 29 A. B. R. 450, 199 Fed. 961 (D. C. N. Mex.): "Now, the discharge of a bankrupt is a collateral matter. If he does not care to be discharged, he need never be, and in that event the estate will nevertheless be closed. His discharge is of no relevancy to the creditors. It is a matter

⁹⁹ *In re Averill*, 1 N. B. N. 544 (Ref. Ohio, affirmed by D. C.). Compare, inferentially contra, *In re Rosenthal & Lehman*, 9 A. B. R. 628, 120 Fed. 848 (D. C. Mo.). Contra, *In re Hitchcock*, 17 A. B. R. 664 (D. C. Hawaii). Obiter, *In re O'Hara*, 21 A. B. R. 508, 171 Fed. 290 (D. C. Pa.). Compare, *In*

re Gillardon, 26 A. B. R. 103, 187 Fed. 289 (D. C. Pa.).

Contra, though obiter, since not allowed under the circumstances in this case, *In re [K. L.] Wong*, 30 A. B. R. 125 (D. C. Hawaii).

As to rule in voluntary bankruptcies, see post, § 2090.

that concerns him and his future, not the estate. I think, therefore, that the cost for this is not to be allowed as part of the compensation of the attorney for the bankrupt, and it will be accordingly disallowed." [This case was even a voluntary case, apparently.]

Analogously (voluntary case), *In re Brundin*, 7 A. B. R. 298 (D. C. Minn.): "It will be observed from the language of the act above quoted that the only allowance of attorney's fees is as part of 'the cost of administration.' It follows that services of an attorney not connected with the administration of the estate are not to be paid out of the estate. The administration of the estate includes the proceedings from the petition until the estate is reduced to money, and the dividends paid and the estate closed. Then the administration ends. In involuntary cases it will be observed that no allowance is made to the bankrupt for attorney's services in resisting the petition, but only while performing the duties required by the act. * * *

"The discharge of the bankrupt, while it will affect his personal rights and obligations, and the rights of his creditors, does not in any way affect the administration of his estate in the court of bankruptcy. It can neither add nor take away a dollar from that estate. The trustee, who administers the estate, and the referee, under whose charge and direction this is done, have nothing to do with the discharge of the bankrupt. The bankrupt may apply for his discharge at the end of one month after the adjudication, and before the administration has passed its preliminary stage, or postpone that matter till the lapse of nearly a year—perhaps months after the administration is ended and the estate closed. The fact that the act requires him to attend the hearing upon his application for discharge is a regulation concerning the matter of discharge alone, which, although a proceeding in bankruptcy, is for the benefit of the bankrupt only, and has nothing to do with the administration of the estate.

"If, by reason of the opposition of some creditor, the services of any attorney may be necessary for the bankrupt, that is his individual concern, and neither reason nor anything in the act suggests that the estate be depleted to furnish him counsel, at the cost of his creditors. Should counsel fees be allowed for services in this case, it must be for the reason that they should be allowed in every case where employed, and would lead to the abuse of needless employment. They would also have to be paid from the estate as well where the bankrupt has committed acts which will prevent his discharge as in the cases where discharge is granted."

Inferentially, *In re Mayers*, 4 A. B. R. 238, 1101 Fed. 695 (D. C. Wis.): "The test for compensation out of the estate is whether the service is rendered in the performance of the bankrupt's duty in aid of the estate and its administration, and not whether the bankrupt stands in need of the service of counsel for his personal benefit and protection in any of the proceedings. No sanction appears in any of the provisions for an allowance in the last mentioned view, and its adoption would violate the general consistency of the act for securing economy in administration. Indeed, the policy of compensating counsel assigned by the courts to aid needy defendants in criminal prosecutions has never been adopted by Congress, and it would seem anomalous to impose the burden of such defense of a bankrupt on the creditors. The opinion recently handed down in the Circuit Court of Appeals for this circuit (*In re Curtis* [4 Am. B. R. 17], 100 Fed. 784), is well in point, both for a general rule of construction to be applied to the act in reference to expenses and for its interpretation of the analogous allowance in the same connection of an attorney's fee to the petitioning creditors in involuntary cases. It is held to be limited strictly 'to the service rendered in procuring the adjudication.' On the construction indicated, the

services rendered in preparing the schedules, and in attendance on the examination of the bankrupt before the referee pursuant to the order, are entitled to an allowance. All other claims are rejected, including that for 'retainer.'"

But compare, *contra*, although the case is not closely reasoned upon this particular point, *In re Kross*, 3 A. B. R. 187, 96 Fed. 816 (D. C. N. Y.): "I am not prepared to say, however, that services as counsel in aid of the bankrupt in litigations over his discharge are to be wholly excluded, when such aid has become necessary without the fault or misconduct of the bankrupt himself. Considering that all attorneys in this country are counselors also, and that the latter term is used in § 60, I should not be inclined to construe the words 'attorney's fee' in § 64 in the narrowest and strictest sense, so as to exclude necessarily such services by counsel as were really required. But, for obvious reasons, claims on this ground should be admitted only most sparingly and with great caution and they should be confined to services during the bankruptcy proceedings itself, excluding previous consultations or advice, as well as all unnecessary attendance as 'counsel' in the course of the proceedings." [This case must have been a case of voluntary bankruptcy, bankrupt's attorney's fees in which are allowable "as the court may direct;" for certainly in involuntary bankruptcies the words of the statute are plain enough that the allowance must be confined to services necessary to assist the bankrupt to perform his statutory duties—it being no part of his statutory duties to file his petition for discharge.]

It would seem to be undoubtedly improper to allow attorney's fees for filing or defending the petition for discharge in involuntary cases; for it is not one of the bankrupt's duties to file such petition nor to defend it. The law simply grants him the privilege of a discharge—it is not a "duty."¹

But, perhaps the bankrupt should be allowed for necessary attorney's fees while in attendance at the hearing upon his application for discharge, such attendance being one of his statutory duties.² What services would be embraced within those rendered necessary by such required attendance does not seem to have been determined. It would be strange, indeed, if creditors should have to pay for the bankrupt's attorney's services in defending the petition for discharge.

§ 2087½. Fees for Services in Connection with Composition Proceedings.—An application to confirm a composition is not a part of the administration of the estate, and, therefore, the bankrupt cannot recover from the estate after denial of confirmation of the composition the sums paid to his attorneys in such proceedings.³

§ 2088. No Allowance for Bankrupt's Admission in Writing of Inability to Pay Debts, etc., nor for Services in Aid of Adjudication; nor in Contests over Exemptions.—No attorney's fees should be

1. *Contra*, and that they may be allowed for discharge petition, *In re Stratemeyer*, 14 A. B. R. 121 (D. C. Hawaii). But compare, *In re Kross*, 3 A. B. R. 187, 96 Fed. 819 (D. C. N. Y.). However, it is evident this was a voluntary bankruptcy, not an involuntary one.

2. *In re Mayer*, 4 A. B. R. 238, 101 Fed. 695 (D. C. Wis.); *In re Stratemeyer*, 14 A. B. R. 121 (D. C. Hawaii). *Contra*, *In re Hammel and Hofman*, 31 A. B. R. 672, 211 Fed. 238 (D. C. N. Y.).

3. *In re Fogarty*, 26 A. B. R. 568, 187 Fed. 773 (C. C. A. Wis.).

allowed for services rendered the bankrupt in a contest over his exemptions,⁴ nor for services pertaining to the adjudication;⁵ nor for services pertaining to the trustee's suits to set aside conveyances made by the bankrupt, nor pertaining to negotiations for compromises thereof;⁶ nor for services pertaining to an order of sale of real estate; nor to questions of the bankrupt's ownership of personal property.⁷

In *re Castleberry*, 16 A. B. R. 430, 143 Fed. 1021 (D. C. Ga.): "Legal services to a bankrupt in having his exemptions allowed is a matter between the bankrupt and his attorneys."

In *re O'Hara*, 21 A. B. R. 508, 171 Fed. 290 (D. C. Pa.): "There was considerable controversy over the exemption, including a hearing before the referee and an appeal to the court; and although the claim in both instances was disallowed, it may well be, that, as between the bankrupt and his attorney, the amount now asked for was fully earned. But the Bankruptcy Act only provides, § 64b, 3, for payment out of the estate of 'one reasonable attorney's fee * * * for professional services actually rendered * * * to the bankrupt in involuntary cases while performing the duties herein prescribed;' evidently referring to those previously enumerated in § 7a. In *re Woodard*, 2 Am. B. R. 692, 95 Fed. 955; In *re Payne*, 18 Am. B. R. 192, 151 Fed. 1018. These are duties which aid in the settlement of the estate, which is no doubt the reason for the allowance to counsel, and among them the endeavor to secure for the bankrupt his exemption claim is not one. In *re Castleberry*, 16 Am. B. R. 430, 143 Fed. 1021. The same is true where the services have to do with obtaining a discharge; which shows the principle involved. In *re Brundin*, 7 Am. B. R. 296, 112 Fed. 306. The exceptions are overruled, and the action of the referee is affirmed."

But services in the preparation of his schedule of exempted property are to be allowed for, for such preparation is one of the bankrupt's duties.⁸

§ 2089. Bankrupt's Attorney's Fee More Discretionary in Voluntary than in Involuntary Cases.—The fee allowable to the bankrupt's attorney is more discretionary in voluntary cases than in involuntary cases.⁹

In purely voluntary cases it may be allowed as the court may see fit.¹⁰

In *re Burrus*, 3 A. B. R. 296, 97 Fed. 926 (D. C. Va.): "The only provision of the Bankruptcy Act regulating the amount to be allowed and paid out of the estate as an attorney's fee in cases of voluntary bankruptcy is found in § 64b, which provides for one 'reasonable fee,' irrespective of the number of attorneys employed. This section evidently intended to and does vest solely in the sound discretion of the court the amount to be allowed under the circumstances of each case."

4. In *re Stratemeyer*, 14 A. B. R. 120 (D. C. Hawaii).

But compare, In *re Christianson*, 23 A. B. R. 710, 175 Fed. 867 (D. C. N. C.), also quoted at § 2079.

5. In *re Stratemeyer*, 14 A. B. R. 120 (D. C. Hawaii).

6. In *re Stratemeyer*, 14 A. B. R. 120 (D. C. Hawaii).

7. In *re Stratemeyer*, 14 A. B. R. 120 (D. C. Hawaii).

8. See ante, §§ 461, 477.

9. In *re* [K. L.] Wong, 30 A. B. R. 125 (D. C. Hawaii). Contra, In *re Beck*, 1 A. B. R. 535, 92 Fed. 889 (D. C. Iowa); contra, In *re Stotts*, 1 A. B. R. 641, 93 Fed. 438 (D. C. Iowa).

10. Bankr. Act, § 64 (b) (3); In *re Smith*, 5 A. B. R. 562, 108 Fed. 39 (D. C. N. Car.); In *re Keller*, 31 A. B. R. 51, 207 Fed. 118 (D. C. N. Y.).

In re Morris, 11 A. B. R. 145, 125 Fed. 841 (D. C. N. Car.): "This court has, by rule, fixed the maximum fee in voluntary proceedings, where there is no unforeseen litigation or extraordinary services, at \$50."

§ 2090. Test in Voluntary Cases, in General.—The test, in voluntary cases, in general is that the services be rendered in assisting the bankrupt to perform his statutory duties and, in addition, such other services may be allowed for as are beneficial to creditors, rendered before any receiver, trustee or marshal is in charge.

Thus, in voluntary cases, the bankrupt should be allowed for legal services rendered to him while he is in the performance of his statutory duties, as in involuntary cases.¹¹

In re Duran Mercantile Co., 29 A. B. R. 450, 199 Fed. 961 (D. C. N. Mex.): "The wording of the statute—Bankruptcy Act, § 64b (3)—is 'for cost of administration,' including an attorney's fee for one attorney for the bankrupt in voluntary cases. When, therefore, we look at the attorney's fee, we must look at it in the light of the question as to whether or not it is 'cost of administration;' that is, whether the services rendered went to the benefit of the estate or the progress of the administration of the estate."

In re Terrill, 4 A. B. R. 625, 103 Fed. 781 (D. C. Vt.): "This is a voluntary case, and the law refers to what services are actually rendered by an attorney for the bankrupt, in assisting him about what the law requires him to do, such as preparing the petition and schedules."

Attorney's fees are allowable for preparing the voluntary petition for adjudication and schedules and for attendance in procuring adjudication.¹²

And in addition thereto, as above stated, he should be allowed for such other services as are beneficial to the estate, rendered before any receiver or trustee or other officer is placed in charge of the estate.¹³

In re Kross, 3 A. B. R. 190, 96 Fed. 819 (D. C. N. Y.): "I have already stated the general nature of the services which I think are designed to be covered by the allowance. In voluntary cases they are such as are indispensable to enable the bankrupt properly to bring his case into bankruptcy, surrender his estate and perform his duties for the benefit of creditors on the one hand, and to receive his discharge if entitled to it, on the other. Section 64 speaks only of an attorney's fee; while § 60, subd. d, uses the word 'counselor' also. The services contemplated by both are doubtless for the most part those of an attorney only, as distinguished from the services of 'counsel.' They include the preparation of the necessary legal papers, procuring the adjudication and reference, bringing the debtor before the referee for such subsequent proceedings as may be required, making in due time the application for discharge, attendance before the judge and referee, as may be needful, and throughout the proceedings keeping himself informed of their progress and giving such attention to the essential steps in the bankrupt's behalf as will secure to him a regular and valid discharge. These are the ordinary attorney's duties."

¹¹. In re Duran Mercantile Co., 29 A. B. R. 450, 199 Fed. 961 (D. C. N. Mex.).

¹². In re Hitchcock, 17 A. B. R. 664 (D. C. Hawaii). Contra, In re Beck 1 A. B. R. 535, 92 Fed. 889 (D. C. Iowa).

Instance, In re Duran Mercantile Co., 29 A. B. R. 450, 199 Fed. 961 (D. C. N. Mex.).

¹³. Obiter, In re [K. L.] Wong, 30 A. B. R. 125 (D. C. Hawaii).

Thus, he may be allowed for services in securing a stay order against the prosecution of a pending attachment suit.

In *re* Duran Mercantile Co., 29 A. B. R. 450, 199 Fed. 961 (D. C. N. Mex.): "Now, as to the next item, the matter of the stay order secured against the attachment proceedings brought by one of the creditors in the District Court of Torrance county, the court's view is that this is compensated properly out of the estate. It goes to the administration of the estate that this suit should be arrested; otherwise, the assets of the estate will be diverted, and not applicable to this proceeding."

Also for procuring a reduction of taxes that would otherwise have been a preferred claim upon the assets and which could not have been as advantageously reduced by the trustee or receiver as by the bankrupt.¹⁴

Probably, though the cases are not in harmony on the point, the bankrupt estate ought not to pay the expense, in a voluntary case, of the bankrupt's getting his discharge, inasmuch as the estate is in no wise benefited thereby and as the bankrupt, at the time of applying for discharge, has presumably gathered enough of a new estate to enable him to defray the expense of procuring his discharge.¹⁵ Such is the undoubted rule in involuntary cases, as we have seen.^{15a}

And services really rendered in the interest of a preferred creditor, especially those rendered after the bankrupt's death, should not be charged against the estate as part of the bankrupt's allowance for attorney's fees.¹⁶

§ 2091. Preliminary Consultations May Be Charged for, in Voluntary Cases.—Consultations in reference to the filing of the bankruptcy petition and the preparation of the schedules may be charged for, in voluntary cases.¹⁷

In *re* Kross, 3 A. B. R. 187, 96 Fed. 819 (D. C. N. Y.): "In voluntary cases, the same schedules are required to accompany the petition, and ordinarily bankrupts are unable to prepare such papers properly, or to comply with the rules and orders pertaining thereto, except by the aid of a professional attorney. This clause of paragraph 3, therefore, indicates the general nature of the services for which a fee is designated to be allowed, viz., those professional services which presumably are necessary and indispensable to the bankrupt to enable him to perform the duties required of him by the act for the benefit of creditors on the one hand, or to secure his own correlative right to discharge on the other."

14. In *re* Duran Mercantile Co., 29 A. B. R. 450, 199 Fed. 961 (D. C. N. Mex.).

15. Compare, § 2079. In *re* Averill, 1 N. B. N. 544 (Ref. Ohio, affirmed by D. C.); In *re* Brundin, 7 A. B. R. 296, 112 Fed. 306 (D. C. Minn.). But compare, contra, In *re* Kross, 3 A. B. R. 187, 96 Fed. 819 (D. C. N. Y.). Also, compare contra, In *re* Christianson, 23 A. B. R. 710, 175 Fed. 867 (D. C. N. C.), quoted at § 2079.

15a. Compare ante, § 2087.

16. In *re* Terrill, 4 A. B. R. 625, 103 Fed. 781 (D. C. Vt.). But compare, In *re* Beck, 1 A. B. R. 535, 92 Fed. 889 (D. C. Iowa), in which the court held the bankrupt, in voluntary cases, to be entitled to attorney's fees only for preserving the estate before the appointment of trustee.

17. In *re* Averill, 1 N. B. News 544 (Ref. Ohio, affirmed by D. C.); contra, In *re* Beck, 1 A. B. R. 535, 92 Fed. 889 (D. C. Iowa); contra, In *re* Stotts, 1 A. B. R. 641, 93 Fed. 438 (D. C. Iowa).

§ 2092. Application for Receiver or Other Provisional Remedy Allowed for.—Applications for the appointment of a receiver, or injunction, and other legal steps necessary to be taken before a trustee is elected by creditors, in caring for the estate, may be allowed for.¹⁸

However, one case holds that the attorney's fees should not as a rule be allowed for mere consultations—that they are to be allowed for services as attorney rather than as counsel, although in some instances counsel fees might be allowed.¹⁹ And another case holds it discretionary with the court in voluntary cases to refuse to allow bankrupt's attorney's fees to be paid out of fraudulently conveyed property that has been recovered by the trustee.²⁰

§ 2093. Only One Fee to Be Allowed.—Only one reasonable attorney's fee shall be allowed;²¹ even though it be in a partnership case and each partner have his own attorney.²²

§ 2094. Bankrupt Paying Attorney in Advance.—The bankrupt, both in voluntary and involuntary bankruptcies, may pay his attorney in advance of the filing of the bankruptcy petition, for services rendered or to be rendered in the proposed bankruptcy.²³ And such prepayment is neither a preference nor fraudulent conveyance.²⁴

In *re Wood & Henderson*, 210 U. S. 246, 20 A. B. R. 1: "This is not a case of a preference, where part of the estate is transferred to a creditor so as to give to him more of the estate than to others of the same class, under § 60 (a) of the Bankruptcy Act. Nor is it a case of a fraudulent conveyance under § 67. It is a transfer in consideration of future services to be reduced if found unreasonable in amount."

§ 2095. All Payments to Attorney in Contemplation of Bankruptcy Governed by § 60 (d).—All payments made before bankruptcy

18. In *re Burrus*, 3 A. B. R. 297, 97 Fed. 926 (D. C. Va.).

19. In *re Kross*, 3 A. B. R. 187, 96 Fed. 816 (D. C. N. Y.), quoted ante, § 2087.

20. In *re O'Connell*, 3 A. B. R. 422, 98 Fed. Rep. 83 (D. C. N. Y.).

21. Bankr. Act, § 64 (b). In *re Eschwege & Cohn*, 8 A. B. R. 282 (Ref. N. Y.).

Assessing Damages on Petitioning Creditor's Bond-Rule Does Not Apply.—Of course, the rules herein laid down apply only to allowances out of the bankrupt estate. Where the petitioning creditors are defeated and no adjudication takes place, the court, in assessing damages upon the petitioning creditors' bond, is not governed thereby as to allowances for attorneys' fees.

22. In *re Eschwege & Cohn*, 8 A. B. R. 282 (Ref. N. Y.).

23. Impliedly, Bankr. Act, § 60 (d). Impliedly, Schedule B. (4).

Bankrupt's Attorney, Employed by Trustee on Re-Opening of Estate, to Collect Old Judgment Obtained by Him before the Bankruptcy, Held to Have No Lien on Amount Collected for Services Rendered before Bankruptcy.—Bankrupt's attorney employed by the trustee to collect an old judgment obtained by him before the bankruptcy but for which he presented no claim for fees against the estate has been held to have no lien on the amount collected nor right to retain the same for the fees earned before the bankruptcy. In *re Blum*, 28 A. B. R. 60, 193 Fed. 304 (D. C. N. Y.). But compare post, § 2677.

24. *Furth v. Stahl*, 10 A. B. R. 442, 205 Pa. 439.

to the attorney in contemplation of the institution of bankruptcy proceedings are to be governed by the provisions of § 60 (d).²⁵

However, payments or prepayments made for other purposes than for the contemplated bankruptcy are not governed by § 60 (d).²⁶

§ 2096. Whether Different Principles Govern from Those Where Allowed Out of Estate.—Whether the prepayment, or security, of attorney's fees previous to bankruptcy is to be regulated by different principles from those governing the allowance of the bankrupt's attorney's fees out of the estate is not clear. Some cases seem to hold that they are not on the same basis and that such prepayments are governed by § 60 (d) and are not limited by § 64 (b);²⁷ while others hold that both are virtually on the same basis.²⁸

In *re Kross*, 3 A. B. R. 187, 96 Fed. 816 (D. C. N. Y.): "The charges to be 'approved' are, I cannot doubt, for the same services which the 'fee' is designed to be allowed for under § 64 (b) par. 3."

Prepayment of attorneys' fees by bankrupts is not favored in bankruptcy, it is said in one case.²⁹

It has been held that § 60 (d) refers only to professional services rendered before the commencement of the bankruptcy proceedings, and not to those rendered during their pendency, the section having been enacted in order to cover those cases which neither could be reached by plenary action, as for a preference, etc. (because, being a prepayment, it could not have been made on a pre-existing debt) nor would be subject to control by way of allowance by the court under § 64 (b) for services during the pendency of the bankruptcy proceedings; the two sections, §§ 60 (d) and 64 (b), together constituting a complete remedy for attorney's fees in regard to the bankruptcy, whether for services rendered before or those rendered after the actual institution of the proceedings.³⁰

In *re Stolp*, 29 A. B. R. 32, 199 Fed. 488 (D. C. Wis.): "In answering the third and fourth questions it must follow that § 70d refers solely to services of

25. Impliedly, In *re Habegger*, 15 A. B. R. 198, 139 Fed. 623 (C. C. A. Minn.).

Haffenberg v. Chicago Title & Trust Co., 27 A. B. R. 708, 192 Fed. 874 (C. C. A. Ills.); whether before or after the services themselves are rendered, held in one case. In *re Cummins*, 28 A. B. R. 385, 196 Fed. 224 (D. C. N. Y.); but held contra, in *re Stolp*, 29 A. B. R. 32, 199 Fed. 488 (D. C. Wis.), quoted at §§ 2096, 2099.

26. Compare post, § 2096; also see In *re Stolp*, 29 A. B. R. 32, 199 Fed. 488 (D. C. Wis.), quoted at § 2096.

27. *Furth v. Stahl*, 10 A. B. R. 442, 205 Pa. 439, rejected in *re Habegger*, 15 A. B. R. 208, 139 Fed. 623 (C. C. A. Minn.), but cited with approval in *re Wood & Henderson*, 20 A. B. R. 1,

210 U. S. 246; *Pratt v. Bothe*, 12 A. B. R. 529, 130 Fed. 670 (C. C. A. Mich.), cited with approval in *re Wood & Henderson*, supra.

28. *Obiter*, In *re Kross*, 3 A. B. R. 187, 96 Fed. 816 (D. C. N. Y.); In *re Lewin*, 4 A. B. R. 634, 103 Fed. 852 (D. C. Vt.).

29. In *re Blanchard*, 20 A. B. R. 417, 161 Fed. 793 (D. C. N. Car.).

30. But, compare, to the effect that § 60 (d) refers to all payments to attorneys for bankrupts, relative to the bankruptcy made before the actual institution of the bankruptcy, whether before or after the services themselves were rendered, In *re Cummins*, 28 A. B. R. 385, 196 Fed. 224 (D. C. N. Y.). In *re Stolp*, 29 A. B. R. 32, 199 Fed. 488 (D. C. Wis.).

the character above described, which were to be and were in fact rendered prior to the bankruptcy. Under former Bankruptcy Acts the question arose repeatedly, whether counsel rendering services prior to bankruptcy, and who had not been paid, should be treated as a general or a preferred creditor; and the uncertainty of receiving adequate compensation as a general creditor would naturally stimulate the practice of paying in advance. Therefore, it being possible to deal with attorneys who are general creditors, or with such as had in fact been paid for past services, in the same manner as other creditors had to be dealt with, § 60d not only embodies a design and remedy to reach the cases where advance payments have been made, but, to be effective, there must be a limit of time within which the contemplated future services are to be rendered. Such limit, as indicated in *Pratt v. Bothe*, supra, is the date of filing the petition in bankruptcy. Judge Severens there said: 'The Bankruptcy Act makes a final and sharply defined line in respect of the power of the bankrupt over his estate and the distribution of it as of the date of the filing of the petition against him. From that time his assets are in gremio legis, and he cannot, unless he compounds with his creditors, bind his assets. He may, of course, make new contracts, and incur new obligations; but they are not chargeable to the funds which have become vested in the trustee until they have subverted the purpose of the bankruptcy proceedings, when, if anything remains, he reacquires it. It would be wholly inconsistent with the scheme of the act that a debtor in contemplation of bankruptcy should be permitted to make an arrangement whereby he should have power, after his assets shall have gone into the hands of the trustee, to alter their disposition by appropriating them to the payment for services thereafter rendered to him, or, indeed, to satisfy the obligations of any executory contract. With respect to services rendered to the bankrupt in the present case after the creditor's petition was filed, it is to be observed that the compensation therefor was not due and owing at the time of the filing of the creditor's petition, and so was not a provable claim. It would be anomalous that the debtor, by preconcert with his attorney, could defeat that provision by an agreement for a benefit to accrue to the bankrupt after the proceedings should be inaugurated, and make the compensation therefor a privileged claim. By section 64b the law provides for compensation to an attorney who assists the bankrupt in performing the duties imposed upon him. But this is done for the purpose of facilitating the proceedings, and for the benefit of the estate. It is not done in recognition of any contract obligation of the bankrupt.'

"Thus, if § 60d is construed as referring to services rendered prior to, and § 64b to services rendered after, the institution of the bankruptcy proceedings, remedies are provided for meeting distinct situations. The cases herein cited, as well as others (see, for example, *In re Kross* [D. C., N. Y.], 3 Am. B. R. 187, 96 Fed. 816; *In re Cummins* [D. C., N. Y.], 28 Am. B. R. 385, 196 Fed. 224) disclose a diversity of opinion upon nearly every phase of these two sections, which, at least as to the character of services covered by § 60d, will probably exist until adjudication by the Supreme Court, or until amendment by Congress. However, if the construction herein will enable the accomplishment of a definite purpose through each section consistent with the general purpose of the Bankruptcy Act, it should prevail rather than a broader construction covering situations which rarely occur, or for meeting which other provisions of the act provide ample remedies.

"The general conclusions are that § 60d refers to the services to be rendered after the time of the payment or transfer; that such services must be germane to the general aims of the Bankruptcy Act; that they must be actually ren-

dered, if at all, before the institution of bankruptcy proceedings, and that the payment or transfer specified in said section cannot apply to services rendered as specified in § 64b; that § 64b refers to services rendered after the bankruptcy proceedings are instituted, to aid the bankrupt in performing his duties under the act.

"In the matter now here for review, the note and mortgage having been given twelve days before bankruptcy ensued, but when the proceedings were contemplated, and it appearing that services were to be rendered and were in fact rendered by the attorney to carry out the contemplated purpose, the referee should have ascertained the reasonable value of the services so rendered, and adjudged the note and mortgage valid as security for the payment thereof; but the value of any service rendered after bankruptcy was not the subject of inquiry upon this proceeding, being determinable only under § 64b." This case is quoted further at § 2099.

Pratt v. Bothe, 12 A. B. R. 535, 130 Fed. 670 (C. C. A. Mich., criticised in *re Habegger*, post, § 2097): "We are of the opinion that § 60 (d): relates to services to be rendered while the debtor is 'in contemplation of bankruptcy,' and not to services to be rendered after bankruptcy proceedings are commenced. * * * The language of the paragraph * * * includes services rendered not only by an attorney, but also those rendered by a 'solicitor in equity or a proctor in admiralty.' This generalization seems to indicate that the services contemplated were such as might be required in general litigation or in the course of the debtor's business, and one cannot help greatly doubting whether Congress 'had in mind the purpose to include those special services which an attorney would render to the bankrupt while in the discharge of his duties, payment for which was provided by another section of the act. It would rather seem that Congress, engaged, as many signs indicate, in guarding the assets of those in contemplation of bankruptcy, to the end that they might be brought without unnecessary expenditure to the hands of the trustee for distribution to creditors, while it would not deny to the debtor the right to employ and pay for legal assistance in his affairs during that critical period, yet proposed a restraint upon that privilege by requiring that such payment should be reasonable in amount—in short, proposed to apply to the incipient stage of bankruptcy the provident economy which it sought to apply to the administration of the bankrupt estate. It may have been thought that there was the same reason for such restraint at that stage of affairs as subsequently. And it is to be observed that the transaction would not become the subject of revision unless bankruptcy ensued. It put attorneys' solicitors and proctors in no worse position than it did some classes of those having business with the debtor."

On the other hand, it has been held that § 60 (d) protects payments made to the bankrupt's attorney before bankruptcy, in contemplation of bankruptcy, whether the payments be made before or after the services were rendered.

In *re Cummins*, 28 A. B. R. 385, 196 Fed. 224 (D. C. N. Y.): "What is meant, by the statute, is that a debtor, under the circumstances therein described, may fully pay an attorney for services to be rendered and it is immaterial whether the payment is made at or after the professional engagement is entered into. Upon the re-examination provided for by the statute, it should not be difficult to determine either the bona fides or the reasonableness of the charge."

Obiter, In *re Kross*, 3 A. B. R. 187, 96 Fed. 816 (D. C. N. Y.): "The charges

to be 'approved' are, I cannot doubt, for the same services which the 'fee' is designed to be allowed for under § 64, subd. b, par. 3. Both paragraphs are to be construed together, so that it becomes immaterial in the result whether the attorney obtains his compensation in the first instance from the bankrupt under § 60, refunding what, if anything, is disallowed by the court, or whether he waits for an allowance by the court under § 64. The latter is evidently the more convenient and desirable practice; and considering that prior payment for an attorney's services to the bankrupt is expressly allowed by § 60, I cannot agree to any such construction of the act as would deprive the attorney of a proper compensation for a necessary service, merely because he did not take it out of the estate at his own estimate in advance." Approved in *In re Habegger*, post, § 2097; disapproved in *Pratt v. Bothe*, supra.

§ 2097. Under § 60 (d) Must Be for Benefit of Estate or in Furtherance of Administration.—The kind of legal services to be performed "in contemplation of bankruptcy" for which an insolvent debtor may contract and make payment in money or by a transfer of property before bankruptcy that will be sustained under the provisions of § 60 (d) are such services as are rendered in aid of the purpose sought to be accomplished by the Act to conserve and benefit the estate of the bankrupt, and thus enure to the benefit of creditors, or are such legal services as are contemplated by the Act in bringing the bankrupt estate before the court, its subsequent administration and distribution to creditors, and the like.³¹

In *re Habegger*, 15 A. B. R. 199, 139 Fed. 623 (C. C. A. Minn.): "Such payments or transfers to an attorney by one contemplating bankruptcy as tend to conserve the estate and bring it before the bankruptcy court for settlement, or other services required by the bankruptcy act to be performed by the bankrupt, are made valid as a preference under that section, to the extent they are found upon examination to be reasonable and equitable; such claims being in principle entitled to equitable priority, as are claims for services performed or property furnished in the preservation and betterment of an estate controlled and administered by a court of equity. * * * If an insolvent contemplating bankruptcy transfers his property, in payment of future legal services to be performed, not beneficial to his estate and which do not inure to the benefit of his creditors, why is such a transfer not a voidable preference or a fraudulent transfer under other provisions of the Act, to the same extent as are other transfers of his property without present consideration?"

Thus, services rendered the bankrupt in opposition to the creditors' petition are not within § 60 (d).

31. In *re Kross*, 3 A. B. R. 187, 96 Fed. 816 (D. C. N. Y.); In *re Lewin*, 4 A. B. R. 634, 103 Fed. 852 (D. C. Vt.). To same effect, compare, In *re Smith*, 5 A. B. R. 559, 108 Fed. 39 (D. C. N. Car.). To same effect, compare, In *re Rosenthal & Lehman*, 9 A. B. R. 626, 120 Fed. 848 (D. C. Mo.). To same effect, *Pratt v. Bothe*, 12 A. B. R. 535, 130 Fed. 670 (C. C. A. Mich.).

Compare, In *re Corbett*, 5 A. B. R. 224, 104 Fed. 872 (D. C. Wis.), where

it is inferable that payment after the filing of the petition but before adjudication, or rather before the court has obtained actual custody of the property used in the payment, might have been held valid if actually made.

But compare arguments in *In re Cummins*, 28 A. B. R. 385, 196 Fed. 224 (D. C. N. Y.), and *In re Stolp*, 29 A. B. R. 32, 199 Fed. 488 (D. C. Wis.), quoted at §§ 2096 and 2099.

§ 2098. Prepaid Fee, to Be "Reasonable" and Subject to Re-Examination.—The fee thus prepaid to the bankrupt's attorney must be reasonable in amount, and the prepayment is subject to re-examination and disapproval by the court.³²

§ 2099. Summary Jurisdiction over Attorney to Require Repayment of Excess.—The court has jurisdiction over the attorney to determine any excessiveness and in proper cases to require repayment by him. Such jurisdiction may be exercised in the bankruptcy proceedings themselves; and its exercise is not violative of the rules regarding the forum for suits against adverse claimants.³³

Nor is it violative of the Seventh Amendment of the Constitution securing the right of trial by jury.

In *re Wood & Henderson*, 210 U. S. 246, 20 A. B. R. 1: "The construction which we have given § 60d does not deprive parties of rights secured under the Seventh Amendment of the Constitution to trials by jury in suits at common law where the value in controversy exceeds twenty dollars. This provision of the constitution extends to rights and remedies peculiarly legal in their nature and such as it was proper to extend in courts of law by the appropriate modes and proceedings of such courts."

Moreover, it is provided for by a special clause of the Bankrupt Act itself.³⁴ Indeed it is the bankruptcy court alone that has jurisdiction to "examine" in such cases, and the state court is without jurisdiction.

In *re Wood & Henderson*, 210 U. S. 246, 20 A. B. R. 1: "Jurisdiction to

³². In *re Wood & Henderson*, 20 A. B. R. 1, 210 U. S. 246; In *re Lewin*, 4 A. B. R. 634, 103 Fed. 852 (D. C. Vt.); In *re Morris*, 11 A. B. R. 145, 125 Fed. 841 (D. C. N. Car.); *obiter*, In *re Kross*, 3 A. B. R. 187, 96 Fed. 816 (D. C. N. Y.); *Pratt v. Bothe*, 12 A. B. R. 535, 130 Fed. 670 (C. C. A. Mich.).

Where the bankrupt and his attorney have scheduled the unpaid fee of the attorney as an unsecured claim and have failed to schedule it among priority claims, it will be denied priority. In *re Morris*, 11 A. B. R. 145, 125 Fed. 841 (D. C. N. Car.). But this decision is not to be regarded as sound. Either the fee was proper or it was not proper; and the mistake of the parties ought not to be irremediable.

Instance, In *re Christianson*, 23 A. B. R. 710, 175 Fed. 867 (D. C. N. C.): "It would be unwise both for creditors and bankrupts to make the compensation so parsimonious that attorneys of standing and experience would be reluctant to act on behalf of bankrupts. If, however, the sums mentioned in the opinion by Judge Brown are to be applied by a hard and fast rule to all

cases, and counsel who accept from bankrupts a larger sum are to be exposed to a citation to return the money to the trustee, and the reflection arising from the fact of receiving as attorney's fees sums forbidden by law, the result can not fail to deter attorneys of reputation and standing from acting on behalf of bankrupts."

³³. In *re Ellis Bros. Printing Co.*, 19 A. B. R. 472, 156 Fed. 430 (D. C. N. Y.), quoted at § 1863; impliedly, In *re Shiebler & Co.*, 20 A. B. R. 777, 163 Fed. 545 (D. C. N. Y.).

Summary Jurisdiction over Bankrupt's Attorneys in General.—Summary jurisdiction exists over bankrupt's attorneys with regard to funds of the bankrupt collected by them even though applied on claims for attorney's fees for services already rendered, In *re Ellis Bros. Printing Co.*, 19 A. B. R. 472, 156 Fed. 430 (D. C. N. Y.).

³⁴ In *re Lewin*, 4 A. B. R. 634, 103 Fed. 852 (D. C. Vt.); In *re Wood & Henderson*, 20 A. B. R. 1, 210 U. S. 246; In *re Lewin*, 4 A. B. R. 634, 103 Fed. 852 (D. C. Vt.), cited with approval in In *re Wood & Henderson*, *supra*.

re-examine the transfer to counsel was certainly not conferred upon any State court. When the statute says that if the transfer in contemplation of filing a petition in bankruptcy shall be found to be excessive it may be reduced by 'the court,' is it possible that it was intended to give the State courts jurisdiction of that much of the administration of the estate, and oust the District Court of the United States, and perhaps delay the settlement of the estate until the State courts of original and appellate jurisdiction shall determine the reasonableness of the counsel fee provided for in contemplation of bankruptcy? The answer to this question is obvious, and clearly against a construction which has this effect upon the system of bankruptcy to be administered in the District Courts of the United States established by the act of Congress. It is true that the State courts under the Bankruptcy Act as it stood before the Amendment of February, 1903, were given jurisdiction to entertain suits to recover preferences to the exclusion of the Federal courts, unless the defendant consented to be sued in the Federal court. *Bardes v. Hawarden Bank*, 178 U. S. 524, 4 Am. B. R. 163. * * * If suit was begun in the State court of Arkansas, that court would have answered, as did the Supreme Court of Missouri in *Swartz v. Frank*, 183 Mo. 439, 82 S. W. 60, the Bankruptcy Act confers no jurisdiction upon a State court to entertain an application of the trustee, or of a creditor to reduce the provision made for counsel, that jurisdiction is given alone to the District Court of the United States administering the property. If the action had been brought in the United States court it would have made the same answer, and, in addition thereto, the jurisdiction of the Circuit or District Court of the United States could have been ousted, prior to the Amendment of 1903, by the defendants withholding their consent to the jurisdiction of the Federal court."

And a plenary suit is not necessary to jurisdiction to determine whether the fee is excessive.³⁵

In *re Wood & Henderson*, 210 U. S. 246, 20 A. B. R. 1: "This section does not undertake to provide for a plenary suit, but for an examination and order in the course of the administration of the estate with a view to permitting only a reasonable amount thereof to be deducted from it because of payments of money or transfers of property to attorneys or counsellors in contemplation of bankruptcy proceedings. There is no provision for the enforcement of this section in another court of bankruptcy, where the bankrupt may be personally served with process in a plenary suit; such court is not given authority to re-examine the transaction. No other court has authority to determine the reasonable amount for which the transaction can stand. *Swartz v. Frank*, 183 Mo. 439."

Such re-examination should be had, however, only on due notice to the attorney concerned.³⁶ Such notice may be by service of a rule or order to appear and show cause served either personally or by mail.

35. But, compare [wherein the court calls such a proceeding if upon petition and notice not a summary but a plenary proceeding], *Haffenberg v. Title & Trust Co.*, 27 A. B. R. 708, 192 Fed. 874 (C. C. A. Ills.).

36. Impliedly, In *re Lewin*, 4 A. B. R. 624, 103 Fed. 852 (D. C. Vt.); In *re Wood & Henderson*, 20 A. B. R. 1, 210 U. S. 246; *Haffenberg v. Chicago Title & Trust Co.*, 27 A. B. R. 708, 192

Fed. 874 (C. C. A. Ills.); *obiter*, *Staunton v. Wooden*, 24 A. B. R. 736, 179 Fed. 61 (C. C. A. Calif.), quoted on other points at § 1705½.

Procedure.—It is said in one case that the procedure should be by motion to fix the allowance and for an order directing the return of the excess, "unless an issue is raised," In *re Shiebler & Co.*, 20 A. B. R. 777, 163 Fed. 545 (D. C. N. Y.).

In *re Wood & Henderson*, 210 U. S. 246, 20 A. B. R. 1: "The section makes no provision for the service of process, and in that view such reasonable notice to the parties affected should be required as is appropriate to the case, and an opportunity should be given them to be heard. We see no reason why notice of the proceedings under § 60d may not be by mail or otherwise, as the court shall direct, so that an opportunity is given to appear in the court where the estate is to be administered and contest the reasonableness of the charges in question."

Perhaps the order reducing the fees should not also command the return of the excess unless the attorney be shown to be able to respond to the demand.³⁷ In the event of his inability so to respond, or of his non-residence, it might be that the order determining the amount of the excess, though binding upon the parties, could not be made finally effectual until a judgment were rendered thereon in a jurisdiction where it could be executed.³⁸

In the subsequent plenary action to make the bankruptcy court's order effective, that order is binding, as *res judicata*, upon the sufficiency of the petition or application presented to the bankruptcy court as the basis of the order, also upon the nature of the transaction between the parties, the ownership of the money, and other questions.³⁹

And where the bankruptcy court decides that the advance payment of attorney's fees constitutes an ordinary preference, rather than an excessive payment under § 60 (d) for services to be rendered prior to the commencement of the bankruptcy proceeding, the proper practice is to dismiss a petition for the re-examination of the payment without prejudice to the right of the trustee to proceed with the remedies provided for the recovery of voidable preferences and fraudulent conveyances, should the transaction be deemed to be one or the other.⁴⁰

The right summarily to re-examine prepaid attorney's fees, under § 60 (d) relates only to services in regard to the contemplated bankruptcy, and payment of fees for other services may not be summarily re-examined, but can be attacked only by plenary action, as for a preference, fraudulent transfer, etc., if susceptible to such attack.

In *re Stolp*, 29 A. B. R. 32, 199 Fed. 488 (D. C. Wis.): "The scope and meaning of these two sections can be determined by ascertaining, if possible, what situations they were designed to meet, what possible evil to remedy, or what right to recognize or protect. The language of 60d, on first reading, appears to place the legal advisers of failing debtors in a class by themselves, to be dealt with according to the prescribed provisions, no matter what the character of the service or when rendered; but, as indicated in *Wood & Henderson*, *supra*, the section was intended to treat with a situation which involved neither a preference nor a fraudulent conveyance. If a payment or transfer for services to be

37. In *re Wood & Henderson*, 20 A. B. R. 1, 210 U. S. 246.

38. *Henderson v. Denious*, 26 A. B. R. 226, 186 Fed. 100 (C. C. A. Ark.).

39. *Henderson v. Denious*, 26 A. B. R. 226, 186 Fed. 100 (C. C. A. Ark.). Compare rules as to extent of the res

judicata of the bankruptcy court's call in the analogous actions by trustees to enforce stockholders' liabilities for unpaid stock subscriptions, ante, § 977.

40. In *re Stolp*, 29 A. B. R. 32, 199 Fed. 488 (D. C. Wis.).

rendered means, as stated (see 210 U. S. 251, 259, 263, 20 Am. B. R. 1, 28 Sup. Ct. 624, 627, 629, 52 L. Ed. 1046), 'in consideration of future services,' 'in expectation of proceedings in bankruptcy,' or 'prepayment,' then the date of the transaction must ordinarily be taken as the commencement of the period during which the contemplated services were 'to be rendered;' and, having reference to the future, the transaction could not be treated as dealing with the ordinary relation of debtor and creditor, in which the latter received payment for a past or present consideration; nor, in view of the relation of attorney and client which has sanctioned compensating attorneys in advance, could it be deemed fraudulent or in fraud of creditors. The section is declared to be *sui generis*, and 'recognizes the temptation of a failing debtor to deal too liberally with his property in employing counsel to protect him in view of financial reverses and probable failure. It recognizes the right of a debtor to have the aid and advice of counsel, and in contemplation of bankruptcy proceedings, which shall strip him of his property, to make provision for reasonable compensation to his counsel, and in view of the circumstances the act makes provision that the court administering the estate may, if the trustee or any creditor question the transaction, re-examine it with a view to a determination of its reasonableness.' Wood & Henderson, *supra*, 210 U. S. 253, 20 Am. B. R. 1, 28 Sup. Ct. 624, 52 L. Ed. 1046.

"It is difficult to see why Congress should have intended by these sections to provide comprehensive remedies to meet all situations which might arise between a debtor and his attorneys, both before and during bankruptcy. There is no reason why an attorney, being a creditor with a matured claim, or a creditor having a claim for past services which the bankrupt has paid, should not at the moment of bankruptcy stand with other creditors; but, when the failing debtor secures counsel and favors him with prepayment for contemplated service, the transaction, being neither preferential nor fraudulent, should, in fairness to creditors, be subject to review by the court. It seems to me that the section is designed to reach the situation which arises out of the desire of both the debtor and his attorney to avoid the necessity of the latter's being charged with having received a preference, or of becoming a general creditor of the estate. It should not be construed to cover other transactions between a debtor and his attorney not fairly within this design, nor within the term of the statute. In other words, it refers to advance payments.

"In meeting the second question, the language of section 60d referring to an attorney, counselor, solicitor in equity, or a proctor in admiralty, presents considerable difficulty. Are the services to be rendered such as pertain to the contemplated bankruptcy, or may they be general professional services rendered by an adviser in any of the several capacities specified? On the one hand, it is argued that, being unrestricted, the language must be given a construction which will cover all situations fairly comprehended within its terms, and it therefore includes all instances where advance payments are made to professional legal advisers, no matter what the character or object of their service may be. On the other, the view is taken that Congress could not reasonably have intended to make a debtor's legal advisers the object of favorable or restrictive legislation, except to the extent that the contemplated service is germane to the general purpose of the bankruptcy law, namely, the subjection of the assets of the debtor to administration and distribution for his creditors.

"In *Pratt v. Bothe* (C. C. A., 6th Cir.), 12 Am. B. R. 529, 130 Fed. 670, 65 C. C. A. 48, it is intimated that the general language referring to solicitors and proctors 'seems to indicate that the services contemplated were such as might be required in general litigation, or in the course of the debtor's business.' This was said in considering whether section 60d referred to services rendered before or after the bankruptcy. On the other hand, the question as to the character of

the services contemplated was directly involved in *In re Habegger* (C. C. A., 8th Cir.), 15 Am. B. R. 198, 139 Fed. 123, 71 C. C. A. 607, 3 Ann. Cas. 276, and it was determined that they were such as were to be rendered in aid of the purpose sought to be accomplished by the Bankruptcy Act, to conserve and benefit the estate of the bankrupt, and therefore inure to the benefit of the creditors; and accordingly a payment or transfer from a failing debtor for services to be rendered in endeavoring to get a composition with creditors, and in defending the failing debtor in a criminal prosecution, was not within the terms of this section. In my judgment the purpose of the section was to meet situations most frequently arising, or likely to arise, and such situations are those arising between a failing debtor and his attorney in respect of services relative to his failing condition or the contemplated bankruptcy. While a failing debtor may have employed, or may wish to employ attorneys for various purposes, it is not probable that the situations in which advance payments are made or are likely to be made, to attorneys for an account other than his involved business affairs or contemplated bankruptcy, occur with sufficient frequency to have been made the object of special legislation. And if this is true, then it is fair to construe the section in question as excluding such other situations. Such section in question provides a new remedy, and, as above indicated, was intended to reach situations which under former bankruptcy acts, and under the present act, could not be reached. It was desired to enable a debtor to pay his attorney in advance, to the end that he might procure the service, and not require such attorney to take the hazzard of payment with general creditors. But a review of the transaction is provided. This appears to be the sounder construction, and should be accepted rather than to presume an intention on the part of Congress to make provisions for all cases where a failing debtor may pay his counsel in advance. It is true that this greatly narrows the language of the act, and, it may be said, eliminates a portion of it. It is also true that it may enable payments to counsel whose services are not to be rendered in furthering the objects of the act, and these will thereafter be permitted to stand, unless possibly they can be attacked as fraudulent. But I think the act should have a construction which will effectuate an intention to deal with situations constantly arising, and which, under the former bankruptcy law, had to be met, either by making the debtor's counsel stand as a general creditor, or by yielding him a priority not awarded by the Bankruptcy Act, or by allowing possible excessive payments in advance to stand.

"I am aware that this restricted view will also affect the application of the remedy provided in section 60d strictly to such cases as appear to be payments for services to be rendered, when such services are admitted or adjudicated to be of the character specified, namely, services germane to the purposes of the Bankruptcy Act; and when it appears that the service to be rendered was not of such a character, the right to review cannot be exercised, but the transaction must either stand or be attacked under some other provision of the Bankruptcy Act." [This case is further quoted at § 2096.]

§ 2100. Prepayment before Filing Petition, or at Any Time before Adjudication.—The bankrupt may make such payment before the filing of the petition; or, perhaps, at any time before adjudication, unless the bankrupt's property be sequestrated by a receiver or marshal, or he be prohibited by an injunction from interfering with it.⁴¹

41. Inferentially, *In re Corbett*, 5 A. B. R. 224, 104 Fed. 872 (D. C. Wis.): In this case the transfer was held not to have passed the title to the attorney because there was no change of posses-

sion. The property was not taken into possession by the attorney until after adjudication. The court summarily ordered return.

However, it has been held that the "prepayment" refers to payment before the bankruptcy proceedings are instituted rather than merely before the services themselves are rendered, so that under this construction a payment to the bankrupt's attorney after services rendered, if before bankruptcy, would come under the control of § 60d and likewise be within the protection of that section so far as any claim of preference might be concerned.⁴²

In *re Cummins*, 28 A. B. R. 385, 196 Fed. 224 (D. C. N. Y.): "The contention of the trustee is in effect that, if a debtor in contemplation of the filing of a petition by or against him retains an attorney to advise and act for him, the attorney must then and there get his fee, else he will become a general creditor. In other words, a lawyer is to be deprived of the safeguard of the statute because he has the decency not to insist on an immediate retainer in money or property, and is willing to wait until he can decide what his fee ought to be in the light of service actually rendered. There is no reason why statutes, under familiar canons, cannot be construed sensibly.

"The Congress has given the court full power to re-examine such a transaction with a view of ascertaining its good faith, and then determining whether the fee is reasonable. What is meant, by the statute, is that a debtor, under the circumstances therein described may fully pay an attorney reasonable compensation for services to be rendered, and it is immaterial whether the payment is made at or after the professional engagement is entered into. Upon the re-examination provided for by the statute, it should not be difficult to determine either the bona fides or the reasonableness of the charge."

§ 2101. Prepayment Effected by Giving Security.—The bankrupt may give security upon his property in advance for his attorney's fees instead of making actual prepayment in cash.⁴³

SUBDIVISION "D."

COMPENSATION OF REFEREE, TRUSTEE AND RECEIVER.

§ 2102. Referee's Compensation.—The referee receives out of the estate, 1st, twenty-five cents for each claim filed for allowance, and, 2nd, one per cent. commission on all disbursements made by the trustee to creditors, if the estate is administered before the referee, or one half of one per cent. on the amount to be paid to creditors, if a composition is effected.⁴⁴

⁴². But see *contra* on this point, *In re Stolp*, 29 A. B. R. 32, 199 Fed. 488 (D. C. Wis.), quoted at § 2096 and 2099.

⁴³. Inferentially, *In re Corbett*, 5 A. B. R. 224, 104 Fed. 872 (D. C. Wis.).

⁴⁴. Bankr. Act, § 40 (a): "Referees shall receive as full compensation for their services, payable after they are rendered, a fee of fifteen dollars deposited with the clerk at the time the petition is filed in each case, except when a fee is not required from a voluntary bankrupt, and twenty-five cents for every proof of claim filed for allow-

ance, to be paid from the estate, if any, as a part of the cost of administration, and from estates which have been administered before them one per centum commissions on all moneys disbursed to creditors by the trustee, or one-half of one per centum on the amount to be paid to creditors upon the confirmation of a composition." "When earned" does not necessarily mean at the time dividends are paid. Compare Supreme Court's General Order XXXV as amended in 1906.

§ 2103. Referee's Commissions Computed on Disbursements to "Creditors."—The commissions of the referee are to be computed only on moneys disbursed to creditors.⁴⁵

In *re Abbey Press*, 13 A. B. R. 15, 134 Fed. 51 (C. C. A. N. Y.): "The referee's commission is upon the amount paid creditors, not necessarily upon the amount collected, which might be largely disbursed in making the collection."

In *re Iowa Falls Mfg. Co.*, 15 A. B. R. 384, 140 Fed. 527 (D. C. Iowa): "The proceeds of the mortgaged property arising from the sale thereof by the sheriff should be excluded from the amount upon which the referee may compute his commissions, and the amount actually disbursed by the trustee to creditors will form the basis of such computation."

Thus, commissions are not to be computed on amounts paid out as expenses for the continuance of business.⁴⁶

Bray v. Johnson, 21 A. B. R. 383, 166 Fed. 57 (D. C. W. Va.): "The precise questions presented for consideration are what compensation, if any, the referee is entitled to receive upon funds handled through the bankrupt's trustees, in conducting the business ordered to be continued by the referee; and what effect should be given to a decree of the court entered making an allowance on account of such compensation to the appellee, and from which no appeal was taken. The first question is one that would seem to be determined by the plain letter of the Bankruptcy Act, and the rules prescribed by the Supreme Court in pursuance thereof. Section 40 of the Act of 1898 on this subject, provided for a commission of one per centum on the sums paid as dividends, or one-half of one per centum on the amount to be paid creditors upon the confirmation of a composition. The act as amended on the 5th of February, 1903, § 40-a, is as follows: [quoting § 40 (a) 166]. The amended section, it will be observed, modifies the language of the original act, which allowed a commission of one per centum on sums paid as dividends, and in addition to otherwise providing largely for the increase of the compensation of referees, authorizes a commission on one per cent. on 'all moneys disbursed to the creditors by the trustee.' This language is clear, and its meaning too plain to admit of controversy. It is as positive as its purpose is apparent, to fix definitely what this judicial officer shall receive from the funds coming under the administration of the court, as to which he might be called upon to take official action. The amendment of 5th of February, 1903, by § 72, emphasized the meaning of the previous provision, and is as follows: 'That neither the referee nor the trustee shall in any form or guise re-

⁴⁵ *Bray v. Johnson*, 21 A. B. R. 383, 166 Fed. 57 (C. C. A. W. Va.), quoted in this section; In *re Philips*, 31 A. B. R. 542, 210 Fed. 889 (C. C. A. Fla.); In *re Rourke Co.*, 31 A. B. R. 788, 209 Fed. 877 (D. C. Tenn.).

Commissions Only on "Dividends" before Amendment of 1903.—Before the Amendment of 1903, his commissions were computed only on "dividends" paid to creditors. In *re Utt*, 5 A. B. R. 383, 105 Fed. 754 (C. C. A. Ills.); In *re Hinckel Brewing Co.*, 10 A. B. R. 692, 124 Fed. 702 (D. C. N. Y.); In *re Goldville Mfg. Co.*, 10 A. B. R. 552, 123 Fed. 579 (D. C. S. C.); In *re Mammoth Pine Lumber Co.*, 8 A.

B. R. 651, 116 Fed. 731 (D. C. Ark.); In *re Ft. Wayne Electric Corp.*, 1 A. B. R. 707, 94 Fed. 109 (D. C. Ind.); In *re Fielding*, 3 A. B. R. 135, 96 Fed. 800 (D. C. Mo.); In *re Barber*, 3 A. B. R. 306, 97 Fed. 547 (D. C. Minn.); In *re Mulhauser Co.*, 9 A. B. R. 80 (Ref. Ohio); In *re Sabine*, 1 A. B. R. 322 (Ref. N. Y.); In *re Coffin*, 2 A. B. R. 344 (Ref. Tex.); In *re Gerson*, 2 A. B. R. 352 (Ref. Pa.). Compare, In *re Gardner*, 4 A. B. R. 420 (Ref. Va.); compare, In *re Anders Push Button Tel. Co.*, 13 A. B. R. 643, 136 Fed. 995 (D. C. N. Y.).

⁴⁶ In *re Rourke Co.*, 31 A. B. R. 788, 209 Fed. 877 (D. C. Tenn.).

ceive, nor shall the court allow them, any other or further compensation for their services than that expressly authorized and prescribed in this act.' Section 2 of the General Orders, No. 35, prescribed by the Supreme Court for the enforcement of the bankruptcy law, also expressly prohibits this charge by the referee, in that it provides that: 'The compensation of referees prescribed by this act shall be in full compensation for all services performed by them under the act, or under these general orders,' but this rule provides for certain expenses which may be allowed by the court. The claim here asserted is clearly not authorized by the original Bankrupt Act, nor under the amendment of February 5th, 1903, and § 72 of the amendments expressly prevents referees from receiving in any 'form or guise' anything other than his statutory compensation, and expressly inhibits the court from making such allowance. The reason why this allowance cannot and should not be made or thought of for a moment, is apparent. The courts are authorized to continue the business of bankrupts, and this referee exercised this authority, which in passing it may be said as to a transaction of this magnitude, without the express sanction of the court, was of exceedingly doubtful propriety, and the issuance of trustees' certificates for \$75,000.00 or indeed for any amount, assuming it should be done in a bankruptcy case at all, ought manifestly not to be thought of by a referee. The temptation, if a referee could thus increase his compensation, to err, would be too great. Serious questions involving his personal interest, upon which he would have judicially to pass, would be continually presented, and the result of such a system would soon be disastrous, and bring the courts of bankruptcy into disrepute. The objections to such an allowance are fundamental, aside from the fact that the compensation is fixed by law. To have the pay of a referee, acting in a purely judicial capacity, respecting a particular transaction, in which he acts for and on behalf of the court, measured by the extent of the fund that might be handled under and in pursuance of decrees and orders entered by himself, would be as anomalous as it would be unfortunate, because of the delicate and embarrassing position in which he would be constantly placed, as manifestly his personal and financial interest in what he was doing would frequently arise, and result in having his best motives impugned. This case affords a striking illustration of why such a thing should not be done, and the consequences that could be expected to flow therefrom. The fund on which a commission can be allowed, as between two referees, is some \$30,000.00 or \$300.00, whereas the claim asserted by one referee is on some \$480,000.00, or for \$4,800.00, being on the amount expended in creating the \$30,000.00, a difference to the referee of \$4,500.00 in his compensation in a single case, as the result of the exercise of his own judicial discretion in deciding to complete partly executed contracts of the bankrupt company. Judicial officers should not be placed in a position where their private interests necessarily become involved in their official action; and should it ever be done to the extent that the view of the bankrupt law contended for by the referee, would bring about, the federal judicial system would sustain a serious blow, and quickly be deprived of its independence, its greatest source of strength with the people and bar. The Bankrupt Act, in our judgment, affords no ground for an interpretation that would be so far reaching in its results, or bring about such serious consequences. It is not intimated or suggested here that the referee was guilty of the slightest impropriety. On the contrary, he was supported in all that he did, by the creditors and trustees, and their counsel, and he expended much time, and performed great labor, showing the utmost fidelity to his trust throughout. But the hazard of such an undertaking as was embarked upon, was too great for a court or referee to enter on. The contracts themselves were of a kind extremely difficult to handle, subject to many

vicissitudes; and while it may have been supposed that considerable money could be realized the result proved how far all such calculations were; \$28,000.00 instead of from \$150,000.00 to \$200,000.00 was realized as the result of more than 18 months' work; and it may be said that this was rather providential."

According to the strict words of the statute, commissions of the referee are not to be computed on the gross amount received by the trustee, nor on all the money paid out by him, but only upon the amounts disbursed by him to creditors (whether lienholding creditors or not), although there seems no reason for making a different rule for the referee from that governing the trustee, whose commissions are computed on the gross disbursements, whether made to creditors or others. There is some force in the contention, moreover, that the word "creditors," as used in § 40, is the correlative of "debts," as used in § 64 (b), referring to costs of administration as "debts" of the estate.⁴⁷

Since the Amendment of 1903 to §§ 40 and 48, a referee is entitled to commissions on all sums, which, but for outside agreement, would be paid through the trustee.⁴⁸

§ 2104. Thus, Commissions on Disbursements to Priority and Secured Creditors.—Thus, commissions are to be computed on taxes, on the priority wages of workmen, clerks and servants, and in short upon all amounts paid to all kinds of creditors,⁴⁹ including secured creditors.⁵⁰

Before the Amendment of 1910 it had come to be held in several cases, though by what appears to have been a narrow construction, that, unless the lienholder invoked the aid of the bankruptcy court, no commissions, either for referee, receiver or trustee could be charged out of the fund

47. Compare, *Gray v. Mercantile Co.*, 14 A. B. R. 784, 138 Fed. 344 (C. C. A. N. Dak.): "Counsel have proceeded on the assumption that a claim which represents expenses or costs of administration is a 'debt or claim' within the meaning of the provision before quoted granting and restricting the right of appeal. The assumption appears to be sustained by the Bankruptcy Act, notably by § 64b; but, if it were not, that would be another reason why there would be no right of appeal from the allowance or rejection of any of the claims other than that of Carroll, which is not of that character."

Compare, inferentially, *In re Curtis*, 4 A. B. R. 17, 100 Fed. 784 (C. C. A. Ills.).

48. *In re Sanford Furn. Mfg. Co.*, 11 A. B. R. 414, 126 Fed. 888 (D. C. N. Car.). But see *In re Anders Push Button Tel. Co.*, 13 A. B. R. 643, 136 Fed. 995 (D. C. N. Y.). And see, *In re Iowa Falls M'fg Co.*, 15 A. B. R. 384, 140 Fed. 527 (D. C. Iowa).

"Disbursements."—As to meaning of

word "disbursements," see *In re Cambridge*, 14 A. B. R. 168, 136 Fed. 983 (D. C. Mass.).

49. *In re Cramond*, 17 A. B. R. 30 (D. C. N. Y.); *In re Coffin*, 2 A. B. R. 344 (Ref. Tex.); *In re Gerson*, 2 A. B. R. 352 (Ref. N. Y.); *In re Force*, 4 A. B. R. 114, 118 (Ref. Mass.); *obiter*, *In re Allison Lumber Co.*, 14 A. B. R. 78, 137 Fed. 643 (D. C. Ga.); *contra*, *In re Anders Push Button Telephone Co.*, 13 A. B. R. 643, 136 Fed. 995 (D. C. N. Y.).

50. *In re Cramond*, 17 A. B. R. 22 (D. C. N. Y.); *Mechanics and materialmen holding liens. Obiter*, *In re Erie Lumber Co.*, 17 A. B. R. 701, 150 Fed. 817 (D. C. Ga.).

However, it must not be forgotten, in cases of sales of property free from encumbrances that each fund is to bear its own burden of the costs, its own burden of the commissions and expenses; and that the commissions on the amounts paid to secured creditors, as such, are to come out of the particular fund on which the security is held.

covered by the lien until the lien was paid in full,⁵¹ on the theory that the lienholder, unless so affirmatively asking aid, was entitled to be paid in full, and that the bankruptcy officials proceeded with a sale practically at their peril, one of the courts saying:⁵²

In *re Harrison*, 24 A. B. R. 715, 179 Fed. 490 (C. C. A. Mo.): "A court of bankruptcy should not assume charge of incumbered property and liquidate the liens on it, unless there are reasonable grounds for believing some advantage will accrue to the bankrupt's estate. If the validity of the liens is unquestioned, and their amount is such that there is probably no excess of value in the property, it should be surrendered to the lienholders or others entitled, unless some other reason appears for retaining control. A court of bankruptcy is not a court of general jurisdiction for the adjudication of controversies or the administration of assets in which the bankrupt's estate is in no wise interested. If, however, cognizance is taken, it should be assumed some benefit or advantage was expected to accrue to the general creditors, and if it results otherwise it is equitable to make the general estate bear the cost of the proceeding. Here the proceeds of sale did not equal the admitted incumbrance, and the deficiency should not be further increased by deducting the commissions of the officers, if there is a general estate against which they can be charged. This is in analogy to the general practice in equity in foreclosure cases, where, if possible, the judgment lien creditors are paid in full, and if a deficiency results from deducting the costs from the proceeds it goes as a judgment against the debtor."

But this line of reasoning was not well founded nor would it operate well in practice. Whilst it is undoubtedly true, as the court says,⁵³ that "if the validity of the liens is unquestioned, and their amount is such that there is probably no excess of value in the property, it should be surrendered to the lienholders or others entitled, unless some other reason appears for retaining control," yet, in actual practice, serious and real uncertainty occurs as to the actual value, arising from the peculiarities of the market or from other circumstances that can only be solved by actually going to sale. Also, frequently, the trustee has a prospective purchaser at the beginning who eventually "backs out." Likewise, frequently, unforeseen legal contingencies occur, causing the original "reasonable" prospect of an excess to disappear. To throw upon the general estate, or upon the court officers in the event there were no such estate, the burden of the costs, expenses and commissions for the care, custody and sale of the particular property so covered by the lien, would be unfair to such officers and unduly burdensome to creditors who usually derive less benefit from the sale of property covered by liens than do the lienholders themselves. To compel trustees in bankruptcy to act in such cases at their personal peril would in a great percentage of actual cases paralyze their efforts, besides having a serious effect on the attitude of the lienholders themselves and prospective pur-

51. Compare post, § 2112; also, see *In re Harrison*, 24 A. B. R. 715, 179 Fed. 490 (C. C. A. Mo.); *Mills v. Virginia-Carolina Lumber Co.*, 20 A. B. R. 750, 164 Fed. 168 (C. C. A. Tenn.).

52. Compare post, § 2112; also see *In re Harrison*, 24 A. B. R. 715, 179 Fed. 490 (C. C. A. Mo.).

53. In *re Harrison*, 24 A. B. R. 715, 179 Fed. 490 (C. C. A. Mo.).

chasers. Doubtless the ruling criticized was in part induced by the abuse sometimes* occurring of taking possession of encumbered property where there is clearly no equity. But it is submitted that the error here consisted in the court's original granting of the order of sale; the court should have ordered the property abandoned. Had the reviewing court put its ruling squarely upon the ground of the abuse of discretion in granting the order (as a careful reading of the case will indicate was the real ground) the case criticized would have been entirely in accord with right principles and would not have laid down a rule which would act as a two edged sword.

Amendment of 1910.—The Amendment of 1910 does not in its terms affect the referee's commissions, but by analogy will indicate the correct rule with regard thereto in the above particulars.

§ 2105. Property Sold Free of Liens When Lienholder Purchaser.—The referee is entitled to commissions upon the full amount of the purchase price disbursed to creditors, even when a lienholding creditor is the purchaser and applies his lien on the purchase price, such method being considered a "disbursement" to a "creditor" notwithstanding the actual money does not pass through the trustee's hands.⁵⁴

Where the mere equity is sold, without the marshalling of liens and the sale of the property free and clear therefrom, with the consequent responsibilities of such proceedings, the commissions of the receiver and trustee, as also of the referee, are only to be computed upon the amount received from such equity. This is entirely different from the case where the property is sold clear and free of liens but the purchaser happens to be a lienholder and applies his lien in part payment. In the latter case it is still a sale clear and free of liens and, equally as in cases of other purchasers, the receiver and trustee are entitled to commissions on the entire amount of the sale and, if the lienholder be also a creditor, the referee likewise is entitled thereto.

Varney v. Harlow, 31 A. B. R. 339, 210 Fed. 824 (C. C. A. Va.): "Subsequent to 1903 and prior to 1910, § 48 allowed trustees commissions on all sums disbursed by them. By the amendments of the later year the allowance was declared to be 'on all moneys disbursed or turned over to any person, including lienholders, by them.' A similar change was made in the provisions of the section fixing the compensation of receivers or marshals. Section 40, dealing with the fees of referees, was left as it had been amended in 1903.

"Does the fact that § 48 was altered by the insertion of the words 'turned over to any person, including lienholders,' while § 40 was not, indicate that Congress wished to make a distinction in this respect between trustees, receivers and marshals on the one hand, and referees on the other? A very vital and important difference was established by the act of 1903. Before that time trustees' commissions, as well as those of referees, were calculated upon the amount paid as

⁵⁴ In *re Sandford Furn. Mfg. Co.*, 11 A. B. R. 414, 126 Fed. 888 (D. C. N. C.). But see *In re Anders Push Button Telephone Co.*, 13 A. B. R. 643, 136 Fed.

995 (D. C. N. Y.); and see, *In re Iowa Falls Mfg. Co.*, 15 A. B. R. 384, 140 Fed. 527 (D. C. Iowa).

dividends and commissions. By the amendatory act of the last mentioned year trustees were allowed commissions on all sums disbursed by them.

"This court has pointed out why it would have been highly inexpedient that any similar provision should have been made as to referees. *Bray v. Johnson* (C. C. A., 4th Cir.), 21 Am. B. R. 383, 166 Fed. 57.

"As we have already seen, the allowance to the latter was increased in another way. The amendment of section 48 made in 1910 was not so much for the purpose of changing the law as it was to settle a question upon which the courts had divided by declaring the agreement of Congress with those decisions which had held trustees entitled to commissions on sums turned over to lienholders. Report No. 691, Senate Judiciary Committee, 2d Session, 61st Congress. It does not seem probable that Congress intended in so indirect a manner to change the construction which had been previously put upon § 40. 2 Remington on Bankruptcy, § 2105.

"It follows that the referee was entitled to the allowance claimed."

The Amendment of 1910 to § 48a provides that trustees and receivers shall have commissions on "money disbursed or turned over to any person including lienholders," but § 40, granting commissions to referees only on "disbursements" to "creditors," was left unchanged, so it was evidently the intention of Congress to make a distinction between the receiver and trustee and the referee as to the allowance of commissions on sales free from liens. The commissions of referees have never been computed upon any other sums than "those disbursed to creditors." And, lienholders may or may not be creditors. If they happen to be creditors and money is disbursed to them, then the referee is entitled to commissions upon such money, the fact of being lienholders not detracting from the attribute of being also creditors. Trustees and receivers, however, by the Amendment of 1910 were given commissions not only on amounts disbursed to creditors, whether lienholders or not, but upon amounts disbursed to any other person, including lienholders who were not creditors. This was the meaning of the framers of this amendment and this is the clear meaning of the section itself. The only difference, however, between the referee's and trustee's rights to commissions relates simply to disbursements made to lienholders (and others) who are not creditors. The trustee and receiver may have, but the referee may not have, commissions on amounts disbursed to lienholders who are not also creditors.

§ 2105½. Also Where Creditor Purchases and Applies Dividend on Price.—Also, the referee is entitled to commissions where a creditor buys in the property and applies his dividends in part payment therefor.⁵⁵

§ 2106. In Composition Cases Referee to Receive One-Half of One Per Cent.—In cases of composition, where the estate is taken away from the trustee and given back to the bankrupt on the bankrupt's paying an

⁵⁵ Impliedly. In *re Morse Iron Works & Dry Dock Co.*, 18 A. B. R. 846, 154 Fed. 214 (D. C. N. Y.).

agreed compensation therefor, the referee, receiver and trustee alike each receive merely one-half of one per cent. commission.⁵⁶

§ 2107. **"Twenty-Five Cents for Each Claim Filed," Part of "Compensation."**—The 25 cents for each claim filed is part of the referee's compensation and is not to be considered as having been added by the Amendment of 1903 by way of reimbursement of expenses. Referees are entitled further to reimbursement of their expenses. The 25 cents for each claim filed is to be paid out of the estate, if there be any estate, as part of the cost of administration. Owing to the ambiguity of the amendment to the statute in this regard, it is not certain whether there can be any charge of 25 cents for each claim filed where there is no estate. It would seem that where there is no estate, there could be no such compensation any more than there could be commissions.⁵⁷

§ 2107½. **Referee Acting as Special Master.**—Where the referee is acting as special master (as he may do in contested adjudications, discharges and compositions, and on applications for injunctions against a court or an officer thereof, and also in independent equity suits for the recovery of transferred property) he is by the weight of authority to be allowed additional compensation, though such additional compensation has been denied him since the Amendment of 1903, by other authorities.⁵⁸

§ 2108. **Trustee's Compensation.**—The trustee receives out of the estate a commission of not to exceed six per cent. on the first five hundred dollars disbursed by him; of four per cent. on the next thousand dollars; two per cent. on the amounts thereafter up to ten thousand dollars, and one per cent. on the balance above ten thousand dollars; but if a composition be made and confirmed, he receives merely one-half of one per cent. on amounts paid to creditors. The trustee also receives a fee of 50 cents out of the estate for the filing of a certificate with the county recorder where the bankrupt owns real estate not exempt.⁶⁰

56. Bankr. Act, § 40 (a).

57. *In re Elk Valley Coal Mining Co.*, 32 A. B. R. 197, 210 Fed. 386 (D. C. Ky.).

58. See ante, § 2011; post, § 2660.

In re Gillardon, 26 A. B. R. 103, 187 Fed. 289 (D. C. Pa.).

When May Referee Be Appointed "Special Master" in Bankruptcy Litigation.—See ante, § 522½.

60. Bankr. Act, § 48 (a): "Trustees shall receive for their services, payable after they are rendered, a fee of five dollars deposited with the clerk at the time the petition is filed in each case, except when a fee is not required from a voluntary bankrupt, and such commissions on all moneys disbursed or turned over to any person, including lienholders, by them, as may be al-

lowed by the courts, not to exceed six per centum on the first five hundred dollars or less, four per centum on moneys in excess of five hundred dollars and less than fifteen hundred dollars, two per centum on moneys in excess of fifteen hundred dollars and less than ten thousand dollars, and one per centum on moneys in excess of ten thousand dollars. And in case of the confirmation of a composition after the trustee has qualified the court may allow him, as compensation, not to exceed one-half of one per centum of the amount to be paid the creditors on such composition."

(b) "In the event of an estate being administered by three trustees instead of one trustee or by successive trustees, the court shall apportion the fees

§ 2108½. **Amendment of 1910—Trustee's Ordinary Compensation.**—The Amendment of 1910 does not change the compensation of the trustee for the performance of his ordinary duties, but leaves such compensation as before, simply making definite and certain that this compensation shall be computed upon amounts paid to lienholders and other persons.⁶¹

§ 2109. **Commissions Computed on Disbursements for Expenses and to Creditors.**—These commissions are figured upon all amounts disbursed by the trustee, whether to unsecured, priority or secured creditors, or in payment of expenses.⁶²

In re Cramond, 17 A. B. R. 29, 145 Fed. 966 (D. C. N. Y.): "The language covers, and evidently was intended to include, all moneys lawfully disbursed by the trustee, and held by him as such, whether to creditors, secured or unsecured or having priority, or to other persons. If to creditors it is immaterial whether the amounts lawfully paid them from the funds in court are paid as dividends or in satisfaction of a lien or liens on the fund. By section 1 of the Act 'creditor shall include anyone who owns a demand or claim provable in bankruptcy.' Secured claims are provable in bankruptcy, although allowable only to a certain amount."

But when the trustee sells securities which are in the possession of a pledgee thereof, he will only be entitled to commissions on the sum realized in excess of the secured indebtedness.

In re Meadows, 29 A. B. R. 165, 199 Fed. 304 (D. C. N. Y.): "What is intended by the term 'disbursed to creditors,' as applied to the compensation of referees, and by the term 'on all sums disbursed,' as applied to the compensation of trustees?"

"The provisions are comprehensive enough to entitle referees to commissions on moneys paid to secured and unsecured creditors (In re Sanford Furniture Mfg. Co. [D. C. N. C.], 11 Am. B. R. 414, 126 Fed. 888), and to allow to trustees commissions on all sums disbursed by them out of the assets of the bankrupt estate, which obviously includes moneys paid for fees and expenses in the administration thereof. When, however, a secured creditor has recourse to a State court to foreclose his lien, or when personal property or securities, without coming into the custody of the bankruptcy court, are sold by pledges under a specific contract of sale, and there is no participation by the pledgees in the proceedings

and commissions between them according to the services actually rendered, so that there shall not be paid to trustees for the administering of any estate a greater amount than one trustee would be entitled to."

Bankr. Act, § 47 (c): "The trustee shall, within thirty days after the adjudication, file a certified copy of the decree of adjudication in the office where conveyances of real estate are recorded in every county where the bankrupt owns real estate not exempt from execution, and pay the fee for such filing, and he shall receive a compensation of fifty cents for each copy

so filed, which, together with the filing fee, shall be paid out of the estate of the bankrupt as a part of the cost and disbursements of the proceedings."

61. See Bankruptcy Act, § 48 (a), as amended in 1910.

62. Obiter. In re Erie Lumber Co., 17 A. B. R. 701, 150 Fed. 817 (D. C. Ga.).

Compare ante, § 2104, for a discussion of those decisions which merely refuse commissions where there has been an abuse of discretion in selling property when there was no reasonable prospect of a surplus over and above valid and unquestioned liens.

of the bankruptcy court, then clearly no commissions are computable on the amounts realized by secured creditors on their securities.

"In the present case, as already pointed out, the pledgees had the right to sell the collateral at public or private sale without notice to the pledgors, and to apply the proceeds to the payment of liabilities. Indeed, the Fidelity Trust Company reserved to itself the right to buy the securities free from any right or equity of redemption in the pledgors. The arrangement with the banks created, not a mere lien, as the referee seemed to think, but a pledge, which carried with it complete control, and the right of sale upon default in the payment of notes for which collateral was given. A lien ordinarily confers no such power, and there is a clear distinction between selling property free from liens, where the title and possession are in the trustee, and selling stocks and bonds pledged to a third party under a written contract.

"In this case it cannot be held that the securities were even constructively in the possession of the trustee. The rights of the pledgees were not affected by the bankruptcy proceedings. As they did not avail themselves of the services of the referee and trustee to sell the securities held by them, they manifestly could not have been compelled to bear any portion of the expenses of the sale, and it is difficult to perceive the validity of the sale by the trustee of personal property which was not in his custody, or in the control of the bankruptcy court, save as to any existing equities of redemption. How could the trustee have immediately delivered the securities to the purchaser, if the pledgees had not voluntarily released them? The pledgees were adverse claimants, and could not have been summarily compelled to surrender their securities, or to submit their rights to the bankruptcy court. Certainly by the mere sale they were not compelled to deliver the collateral to the trustee. If the proceeds of the sale had been insufficient to pay the pledgees, not only would the trustee have been unable to make delivery of the securities to the buyer, but the pledgees would doubtless themselves have sold under their contract.

"The authorities in support of the contention of the trustee, and upon which the referee placed reliance, are clearly distinguishable."

The rule laid down in this paragraph, § 2109, is not changed by the Amendment of 1910. On the contrary, that amendment enunciates the rule expressly, allowing commissions on all amounts disbursed or turned over to any person, including lienholders.⁶³

In *re Howard*, 31 A. B. R. 251, 207 Fed. 402 (D. C. N. Y.): "There was a division of opinion whether or not this gave commissions to trustees on moneys received by them and disbursed by them which were derived from the sales of mortgaged property and which moneys were covered by and properly applicable to the payment of the lien. Since the amendatory act of 1910 section 48-a provides that trustees shall receive 'such commissions on all moneys disbursed or turned over to any person, including lienholders, by them, as may be allowed,' etc. This amendment settled the disputed questions as to the effect of the amendment of 1903, so far as trustees are concerned."

§ 2110. Except That in Composition Cases Computed Only on Disbursements to Creditors.—But in composition cases, the trustee is entitled to commissions only on disbursements to creditors, and then only at the rate of one-half of one per cent. and only in case he shall have

63. See Bankr. Act, § 48 (a), as amended in 1910.

qualified as trustee before confirmation of the composition.⁶⁴

The Amendment of 1910 to Bankruptcy Act, § 48, has not changed this rule, save and except that the trustee may also be allowed additional compensation where he has conducted the business of the bankrupt,⁶⁵ such additional compensation being allowable up to a further one-half of one per cent. upon the amounts disbursed to creditors.

The same manner of computation and rate of commissions in composition cases, prevails in allowances to receivers, by the Amendment of 1910.

§ 2111. Whether "Disbursement" Includes Proceeds of Property and Trust Funds Surrendered to Adverse Claimants, and Exempt Property Sold by Trustee.—Perhaps, even before the Amendment of 1910, "disbursed" included the proceeds of the sale of property surrendered to adverse claimants in lieu of the specific property itself and trust funds traced into the trustee's hands and surrendered.⁶⁶

Compare instance and reasoning before the Amendment of 1910, wherein expense and compensation for care and custody in preserving specific property were taxed against an unsuccessful claimant; *In re Schocket*, 24 A. B. R. 47, 177 Fed. 583 (D. C. R. I.): "Blankenstein's petition prayed for a return to him of specific personal property which was in the hands of a receiver when he filed his petition, and which subsequently came into the hands of the trustee upon his appointment. The relief sought—i. e., a return of specific property—was inconsistent with a sale by the trustee. Neither Blankenstein nor the trustee made application for a sale of the property and to hold the proceeds in lieu thereof. The trustee contends that the reclamation proceedings prevented a sale and gave rise to expenses in preserving the property; that these expenses were the result of a fraudulent claim, and should not be cast upon the estate, but should be borne by the petitioner for reclamation and taxed against him. While it is doubtful if this expense falls strictly within the usual meaning of the term 'costs of suit,' and while no statutory provision in terms covers a charge of this character, yet in a proceeding in equity the taxation of similar charges seems to have been allowed. In *Burns v. Rosenstein*, 135 U. S. 449, 10 Sup. Ct. 817, 34 L. Ed. 193, which related to proceedings in equity, the court said: 'The allegations of the original bill justified the issuing of the attachment. It was right that the property taken under it should be cared for, and, as the court found that the plaintiffs were entitled to a decree against the defendants, a judgment for costs properly followed; and we perceive no reason why the plaintiffs should not have been allowed, as part of their costs, a reasonable amount for the expenses incurred in preserving the attached party, and for which they became primarily liable to the officer keeping it. We cannot say, upon the record before us, that the court below exceeded its discretion in apportioning the expenses thus incurred.' A court of equity, in extending an order for the taxation of costs so that it may include charges and expenses properly incurred, seems to proceed rather upon considerations of the substantial equities of the parties than upon ordinary statutory provisions concerning costs. 3 Daniell's Chancery (1st Am. Ed.), p. 1586. The petitioner in reclamation having made application to a court exercising chancery powers in the administration of the bankrupt's assets,

64. Bankr. Act, § 48 (a).

65. See Bankr. Act, § 48 (a) and (e), as amended in 1910.

66. Inferentially, *In re Cambridge*, 14 A. B. R. 168, 136 Fed. 983 (D. C. Mass.).

seeking a determination of his right to have returned to him specific property held by the trustee for the benefit of the creditors, is justly chargeable for such necessary expenses in the custody of the goods as were occasioned by the proceedings instituted by him, and which would not have been incurred but for his intervention. To cast upon the property belonging to the creditors the costs of preservation pending the fraudulent claim of an intervener is contrary to equity. I am of the opinion that the court has authority to so extend an order for the taxation of costs against the intervener as to include a direction to tax charges and expenses of custody, as well as ordinary costs. Such charges and expenses should cover only the custody and expense which were the direct result of the intervention proceedings. Charges for expense of keeping, that would have been necessary irrespective of the filing of the reclamation proceedings, should be disallowed."

The Amendment of 1910 places beyond doubt the right of the trustee to commissions upon the proceeds of property and trust funds surrendered to adverse claimants, such amendment providing for "commissions on all moneys disbursed or turned over to any person, including lienholders, by them, etc."

Notwithstanding the breadth of the term used, it is still doubtful whether commissions to "any person" should be held to include commissions on exempt property where it has been sold by consent, since § 48 should be read in connection with other sections in *pari materia*, such as § 6, wherein it is provided that "this act shall not affect the allowance to bankrupts of the exemptions which are prescribed by the state laws in force, etc." Furthermore, § 48, in this regard is to be read in the light of the well-known policy of the law, as expressed in the decisions, of great liberality towards debtors in the allowance of exemptions.⁶⁷

However, where exempt property is sold by the trustee, there is considerable justification for charging commissions therefrom against the bankrupt, since he has received the benefit of the trustee's work in this regard,⁶⁸ and it may be that the courts will charge commissions upon exempt property where it has been sold by the trustee either for the sole benefit of the bankrupt, or for the conjoint benefit of the bankrupt and creditors. In no event, however, can commissions be charged upon exempt property set over to the bankrupt "in kind."

§ 2112. Entitled Even Where Outside Agreement to "Credit" Exists and Actual Money Does Not Pass.—And the trustee, similarly to the referee [ante, § 2105], is entitled to commissions upon all amounts that would be disbursed by him but for outside agreement between the parties, as, for instance, where a lienholder buys in the property and applies his debt on the purchase price, etc.,⁷⁰ or where a creditor buys it in and credits

⁶⁷. See ante, § 1093½.

⁶⁸. Inferentially, *In re Castleberry*, 16 A. B. R. 431, 133 Fed. 821 (D. C. Ga.).

⁷⁰. *In re Sanford Furn. Mfg. Co.*, 11

A. B. R. 414, 126 Fed. 888 (D. C. N. C.).

Compare, contra, before Amendment of 1903, *In re Kaiser*, 8 A. B. R. 108 (D. C. Mont.), where the rule is laid down

his dividends thereon.⁷¹

This does not apply where merely the equity of redemption is sold. It only applies where the property is sold clear and free of encumbrances and the liens are transferred to the proceeds of sale. In the latter cases, of course, if one of the lienholders is a purchaser he may apply his interest in the proceeds as lienholder in payment of the purchase price, for it would be a vain thing to have him pay in the money and then have the trustee pay it out to him directly; in such cases, commissions should be computed upon the lien thus applied precisely as if some other person were the purchaser. However, this doctrine only would apply to sales made clear and free of encumbrances. It would not apply to the sale of an equity of redemption, for in the latter instance the estate is not sold but only the reversion in the estate; moreover, there would be no basis for allowance to the receiver or trustee where merely the equity were sold, for the compensation allowable to the receiver and trustee is for their care and responsibility in regard to the entire estate and for the marshalling of liens and determination of priorities therein and for the getting of a purchaser for the entire value. In other words, it is absolutely essential to the right of commissions in such instances that the sale be in fact a sale clear and free of encumbrances with transfer of the rights of the lienholder to the proceeds of sale.

The Amendment of 1910 would not affect the doctrine of this paragraph. So far as the doctrine relates to referees it is rather restricted by the amendment. Before the amendment the trustee was entitled to commissions on sums disbursed to lienholders only in the event the lienholders were also creditors of the bankrupt. To cover this manifest injustice, the amendment of 1910 provides that where the lienholder is not a creditor and yet receives

that he is not entitled to commissions unless it actually does pass through his hands. This case, however, was decided before the Amendment of 1903. In this instance a great hardship was suffered by the trustee. He had at the instance of creditors instituted suit against third parties for the recovery of certain assets. The creditors then sold out their claims to a third party and the case was dismissed. The purchase price was probably the result of the trustee's suit and it seems highly unfair that the trustee should be deprived of his commissions through this outside settlement.

Apparently contra, and that he is not entitled to require a secured creditor whose lien was created more than four months prior to bankruptcy and has been satisfied in full, to pay such commissions on the amount received by him, *In re Anders Push Button Telephone Co.*, 13 A. B. R. 643, 136 Fed. 995 (D. C. N. Y.). With regard to this case of *In re Anders*, two things are to

be observed, first, that the secured creditor had already been paid his claim in full and this was an effort to make him pay commissions afterwards. While this fact would not alter the principles involved yet it would nevertheless tend to confuse the issue, and, second, that it appears there was enough in the fund thus covered by the lien to pay the costs, without touching the lien. Manifestly, the costs should first be paid, then the liens in full, in the order of priority.

[Before Amendment of 1910] Apparently contra, *In re Harrison*, 24 A. B. R. 719, 179 Fed. 490 (C. C. A. Mo.), but in reality holding that commissions are not to be charged out of the fund until lienholders are paid in full unless they invoke the aid of the court or the lien is disputed—a ruling, by the way, to be seriously questioned on principle, compare § 2104.

71. *In re Morse Iron Works & Dry Dock Co.*, 18 A. B. R. 846, 154 Fed. 214 (D. C. N. Y.).

the proceeds of his lien through the efforts of the trustee and receiver, then the trustee and receiver shall be entitled to commissions thereon. The referee's commissions, however, were not affected by the Amendment of 1910 and therefore would not be computed upon disbursements to lienholders unless such lienholders were also "creditors."

§ 2113. No Absolute Right to Full Commissions: Less May Be Allowed or All Allowance Withheld.—The trustee has not the absolute right to the full commission: The court may allow him less. The only limitation prescribed by the statute is a maximum limit: the court shall not allow him more than six per cent. on the first five hundred dollars, nor more than four per cent. on the next thousand, etc.

The court may, in its discretion, withhold all compensation from any trustee who has been removed for cause.⁷²

By this provision of clause (c) it should not be inferred that the court may not withhold all compensation to the trustee for other causes than his removal. It is not a place for the application of the rule "*Inclusio unius, exclusio alterius*." Circumstances may be such as to warrant refusal of compensation altogether, even though the trustee be not removed. The discretion not to grant the maximum compensation is the discretion to refuse compensation altogether, for cause.⁷³

In *re Schoenfeld*, 25 A. B. R. 748, 183 Fed. 219 (C. C. A. Pa.): "Where a receiver or trustee has been negligent in the performance of his duty, the court may, in a proper case, without the filing of exceptions deny him any commissions."

The doctrine of this paragraph is not affected by the Amendment of 1910.

See Report No. 691 of the Judiciary Committee of the Senate, 61st Congress, Second Session: "Of course, the rates of commissions prescribed are maximum limitations. Less, but not more, may be allowed; and it is hoped the courts will exercise their discretion still in allowing less amounts where proper."

§ 2114. Apportionment, Where Three Trustees or Successive Trustees.—In the event of any estate being administered by three trustees instead of one trustee, or by successive trustees, the court will apportion the fees and commissions between them according to the services actually rendered, so that there shall not be paid to trustees for the administering of any estate a greater amount than one trustee would be entitled to.⁷⁴

⁷² Bankr. Act, § 48 (c). In *re Lev-erton*, 19 A. B. R. 434, 155 Fed. 925 (D. C. Pa.). See ante, § 947½.

Surcharging Trustee. — Instance, surcharging of trustee for delivering over to an adverse claimant firm of which he was a member, a crop of rice of which the bankrupts were in

possession "as agents" at the time of the bankruptcy. *Hebert v. Crawford*, 228 U. S. 204, 30 A. B. R. 24, quoted on other points at § 1807.

⁷³ Similarly as to receiver, In *re Tisch*, 29 A. B. R. 339, 202 Fed. 1018 (D. C. N. Y.).

⁷⁴ Bankr. Act, § 48 (b).

§ 2115. Extra Compensation for Conducting Business.—Trustees and receivers are entitled to extra compensation for continuing the business of the bankrupt.⁷⁵

Before the amendment of 1903 a great injustice was done to trustees who were required to continue the business. It was repeatedly held, and entirely in accordance with the law, that no extra compensation could be allowed for such additional services.⁷⁶

The framers of the Amending Act of 1903, although in a somewhat ineffective way, endeavored to remedy this defect. They provided by amendment to clause 5 of § 2 that courts of bankruptcy should have power to "authorize the business of bankrupts to be conducted for limited periods by receivers, the marshal or trustees, if necessary in the best interests of the estate, and allow such officers additional compensation for such services, but not at a greater rate than in this Act is allowed trustees for similar services."⁷⁷

The Amendment of 1910 permits additional compensation to trustees and receivers (and marshals) for continuing the business of the bankrupt and specifies the extent and the manner of the fixing thereof.^{77a}

See Report No. 691 of the Senate Judiciary Committee of the 61st Congress, 2nd Session: "As the law originally stood there was no provision whatever regulating the compensation of receivers, although the compensation of trustees (at any rate for the performance of their ordinary duties) was most carefully and economically prescribed and limited. The idea of the framers of the law of 1898 undoubtedly was that the administration of bankrupt estates would be placed in the hands of trustees who were to be elected by creditors and whose

⁷⁵. Bankr. Act, § 2 (5); *In re Pequod Brew. Co.*, 18 A. B. R. 352 (Ref. N. Y.); *In re Shiebler & Co.*, 23 A. B. R. 162, 174 Fed. 336 (C. C. A. N. Y.); compare, *In re Russell Card Co.*, 23 A. B. R. 300, 174 Fed. 202 (D. C. N. J.).

⁷⁶. *In re Epstein*, 6 A. B. R. 191, 109 Fed. 878 (D. C. Ark.). Contra, *In re Plummer*, 3 A. B. R. 320 (Ref. N. Y.), criticised and disapproved in *In re Epstein*, 6 A. B. R. 191, 109 Fed. 878 (D. C. Ark.).

⁷⁷. *In re Dimm & Co.*, 17 A. B. R. 119 (D. C. Pa.): Daily auction sales held to be within the amendment. Obiter, *In re Kirkpatrick*, 17 A. B. R. 594, 148 Fed. 811 (C. C. A. Mich.).

^{77a}. See Bankr. Act, § 48: "(e) Where the business is conducted by trustees, marshals, or receivers, as provided in clause five of section two of this act, the court may allow such officers additional compensation for such services by way of commissions upon the moneys disbursed or turned over to any person, including lien holders, by them, and, in cases of receivers or marshals, also upon the

moneys turned over by them or afterwards realized by the trustees from property turned over in kind by them to the trustees; such commissions not to exceed six per centum on the first five hundred dollars or less, four per centum on moneys in excess of five hundred dollars and less than one thousand five hundred dollars, two per centum on moneys in excess of one thousand five hundred dollars, and one per centum on moneys in excess of ten thousand dollars: Provided, That in case of the confirmation of a composition such commissions shall not exceed one-half of one per centum of the amount to be paid creditors on such composition: Provided further, That before the allowance of compensation notice of application therefor, specifying the amount asked, shall be given to creditors in the manner indicated in section fifty-eight of this act."

As to what does not amount to "carrying on the business," see *In re Knosher & Co.*, 28 A. B. R. 747, 197 Fed. 136 (C. C. A. Wash.), quoted at § 2119½.

compensation was carefully limited. However, it was necessary to provide for the contingency, frequently occurring, of a period of time elapsing after the filing of the petition in bankruptcy and before the election of the trustee, during which interval assets might be in danger of destruction or depreciation, and for this purpose it was provided that receivers might be appointed 'when absolutely necessary for the preservation of the estate,' and that these receivers (as well as the trustees afterwards) might carry on the business whenever the best interests of the parties required it, though only for 'limited periods.' While the compensation of trustees (at least their 'ordinary' compensation) was carefully limited, yet the compensation of receivers was left wholly to the discretion of the court, a defect which the Amendment of 1903 did not correct. Such unlimited discretion in the allowance of compensation has offered opportunity for certain serious abuses to creep in. Indeed, in some sections of the country, the appointment of receivers and the conducting of the business by them have become the rule rather than the intended exception, a custom which has resulted in estates being kept for prolonged periods, sometimes, indeed, for almost their entire administration, in the hands of receivers appointed by the courts, with compensation allowable in the unlimited discretion of the courts, rather than in the hands of trustees elected by creditors, with compensation carefully and economically limited. As to the matter of additional compensation for the conducting of the business by the receiver or trustee, the Act of 1898, as originally passed, gave no such additional compensation. This was an injustice, because the conducting of the business of the insolvent is frequently necessary, particularly when adjudications are contested or when the assets consist of an active business which can be best sold as a going concern. The Amendment of 1903 sought to correct this injustice by an amendment of § 2, clause 5, of the act—a part of the statute, however, which is not germane to the subject of compensation, for which reason the whole subject is now referred to § 48 of the act. Through the unfortunate wording of the Amendment of 1903, especially through the use of the word 'similar,' this clause regarding compensation was at least ambiguous. It was the actual intention of the framers of the Amendment of 1903 that where the trustee or receiver conducted the business he might be allowed additional compensation, but that such additional compensation should not exceed once again the compensation prescribed in § 48. § 48 carefully limiting the compensation of the trustee to certain fixed percentages upon moneys disbursed. The courts have construed the Amendment of 1903 as allowing additional compensation for conducting the business, to be sure, but have held that there is no limit upon the amount allowable, save and except in the 'discretion of the court.' (In re Shiebler & Co., 23 A. B. R. 162; 174 Fed. 336.) A careful reading of the proposed amendments forming new clauses (d) and (e) of § 48, in conjunction with § 48 (a) of the law as the latter clause continues to stand [§ 48 (a) is itself recommended for amendment, as hereinafter noted], will exhibit fully the method proposed to be adopted by the present amendment for compensating receivers for their ordinary duties and for giving additional compensation to trustees or receivers for the conducting of business. As a basis from which to start, the established rate of compensation already prescribed in § 48 (a) of the act for trustees for the performance of their ordinary duties is adopted. Trustees or their ordinary services already are compensated in § 48 (a) of the act by way of commissions on moneys actually disbursed by them, the rate being 6 per cent on the first \$500, 4 per cent on the next \$1,000, 2 per cent on the next \$8,500, and 1 per cent above \$10,000, averaging, in an estate of \$5,000, less than 3 per cent on the whole; in an estate of \$10,000, less than 2½ per cent on the whole; and in an

estate of \$20,000, less than 2 per cent—a very low rate of commission. The present amendment fixes the maximum compensation that can be allowed receivers for the performance of their ordinary duties at precisely this same rate, instead of leaving it to the unlimited discretion of the court. It also fixes the extra compensation, whether it be to the receiver or trustee, for the conducting of the business, to once again this same rate; so that, at best, the ordinary and extraordinary compensation taken together, in the event that both a receiver and trustee have successively had charge of the estate and even have both conducted the business, cannot exceed four times the amount allowable to trustees by § 48 (a) of the act for the performance of his ordinary duties. The practical difficulty in the way of allowing commissions to receivers, where the receivers turn over to the trustee in specie the property which they have been taking care of, is obviated by the provision that the commissions are to be figured upon the amounts thereafter actually realized upon sale of such property so turned over in specie. Thus the bill seeks to reduce to the one rational basis of commissions, on moneys actually realized, the compensation, both ordinary and extraordinary, of both trustee and receiver; and by this is done away with, also, the unlimited discretion of the courts in the allowance of compensation to such officers. Of course, the rates of commission prescribed are maximum limitations. Less, but not more, may be allowed, and it is hoped the courts will exercise their discretion still in allowing less amounts where proper. It is further to be observed that creditors are to be given notice of all applications for allowance, and thus there is afforded an additional safeguard. The changes proposed by §§ 1, 9, of the amendatory bill will then, it is thought, tend to prevent extravagance in the administration of insolvent estates and to remove the temptation which now exists toward the creation of prolonged receiverships, and will also tend to put the administration of bankrupt estates promptly into the hands of trustees elected by the creditors, in accordance with the actual design of the framers of the bankruptcy act, rather than in the hands of receivers appointed by the courts."

§ 2117. No Additional Compensation Allowable "in Any Form or Guise."—The statute, in § 72, provides that "neither the referee, receiver, marshal nor trustee shall, in any form or guise, receive, nor shall the court allow him, any other or further compensation for his services than that expressly authorized and prescribed in the act."⁷⁸

⁷⁸ See ante, § 2011; "Policy of Act That of Strictest Economy in Expenses and Costs of Administration."

In re Meadows, 29 A. B. R. 165, 199 Fed. 304 (D. C. N. Y.); De Vries v. Orem, 17 A. B. R. 876, 65 Atl. 430 (Md. Ct. App.); In re Screws, 17 A. B. R. 269, 147 Fed. 989 (D. C. Ga.); In re Epstein, 6 A. B. R. 191, 109 Fed. 878 (D. C. Ark.).

In re Pierce, 6 A. B. R. 747, 111 Fed. 516 (D. C. Colo.): Referee allowed himself per diems for taking testimony, also fees for subpoenas, orders, etc.: Court disapproved.

In re Carolina Cooperage Co., 3 A. B. R. 154, 96 Fed. 950 (D. C. N. C.); In re Troth, 4 A. B. R. 780 (D. C.

Ohio); In re Kaiser, 8 A. B. R. 108, 112 Fed. 955 (D. C. Mont.); In re Barker, 7 A. B. R. 132, 111 Fed. 501 (D. C. Iowa).

But compare instance of clear violation of this provision, In re Hart & Co., 18 A. B. R. 137 (D. C. Hawaii), in which the referee was allowed "extra" compensation for attending to the trustee's inquiries in conducting the business.

Appointing referee as special master to hear an application for an order upon the bankrupt to surrender assets: In re Herskovitz, 18 A. B. R. 247, 152 Fed. 316 (D. C. N. Y.).

District Clerk's Compensation.—Clerk can not charge for issuing sub-

In *re Halbert*, 13 A. B. R. 399, 134 Fed. 236 (C. C. A. N. Y.): "This language is so precise, so unambiguous and so explicit as to preclude the allowance of additional compensation upon any theory of a dual personality."

In *re Coventry Evans Furn. Co.*, 22 A. B. R. 623, 166 Fed. 516, 171 Fed. 673 (D. C. N. Y.): "Prior to the amendment it was customary to make extra allowances to trustees and this was in some cases upheld; but it is seen that the amendment is prohibitory on the court, and absolutely bars all such allowances, however onerous, meritorious, and valuable the services of the trustee."

And a contract to give extra compensation is void on the ground of public policy.

DeVries v. Orem, 17 A. B. R. 879, 65 Atl. 430 (Md. Ct. App.): "So it appears from a review of the acts of Congress on this subject, and from the authorities construing them, that it would manifestly be in violation of the spirit and intent, as well as the plain language of the acts, to allow extra compensation to a trustee for his services in bankruptcy cases. But, independent of the acts of Congress relating to bankrupt estates, we are of the opinion that contracts of this character should not be enforced, and are void as against public policy.

"In this case the appellee was an unsecured creditor of the estate to an extent of \$200,000, and owning more than over 90 per cent. of the unsecured claims. The unsecured indebtedness amounted to about the sum of \$217,000. The dividend she was to receive on account of her claims was pledged to the appellant for the payment of a commission of five per cent. on the entire proceeds of the sales of the assets of the estate. In other words, she agreed to pay him for his services as trustee an additional sum to the compensation he would receive under the Bankrupt Acts that would equal a commission of five per cent. on the entire sales. And this commission was to be paid on the entire proceeds of sales including the mortgaged property, and also the amount to be allowed the secured creditors. A trustee is an officer of the court and is appointed for the purpose of acting for the interests of all the creditors, without favor or partiality. And no contract between him and a creditor should be upheld which is calculated to improperly influence his action, or which would tend to make it to his interest to favor one creditor over another. The principle is well settled that no man should be allowed to have an interest in conflict with or against his duty. He certainly should not be allowed by his own act voluntarily to create such an interest. * * * The authorities sustain the proposition in cases similar to the one at bar, that contracts of this character are illegal and against sound public policy. In *Cowing v. Altman*, 1 Thomp. & Cook (N. Y.) 494, where the consideration for a check was an allowance or promise agreed to be paid the payee thereof for his services as an assignee in bankruptcy over and above the fees and commissions allowed by law, and in express violation of the United States Bankrupt Act, it was held that the consideration was illegal and the check void."

The Amendment of 1910, to § 72, it will be observed, includes the receiver and marshal among those thus prohibited.

pœnas: In *re Pierce*, 6 A. B. R. 747, 111 Fed. 516 (D. C. Colo.).

But the clerk is entitled to reimbursement for his expenses necessarily incurred in publishing and mailing notices where he performs such duty. In

re Hardware & Furn. Co., 14 A. B. R. 186, 134 Fed. 997 (D. C. N. Car.).

And may charge so much for each notice, not as a fee, but to cover such expense: In *re Hardware & Furn. Co.*, 14 A. B. R. 186, 134 Fed. 997 (D. C. N. Car.).

Of course this prohibition refers only to allowance of compensation out of assets and would not refer to costs taxed against unsuccessful petitioning creditors, in favor of receivers or marshals where no adjudication occurs and no moneys are realized in the estate. The Amendment of 1910 in this regard, should, of course, be construed in the light of the evils it sought to correct, which were extravagance and uncertainty in the allowance of compensation out of assets in process of administration—not to the taxing of costs against unsuccessful parties litigant.

Likewise, the ordinary fees of the marshal for the service of papers, etc., are governed by § 52 (b) of the Act and are not within the contemplation of § 48.⁷⁹

In cases where there is no adjudication and no composition under § 12a, but where there is a dismissal of the petition without adjudication, and without judgment against the petitioning creditors, as, for example, in cases of "friendly settlements" where the entire bankruptcy proceedings are "lifted" by consent of all creditors, of course, the compensation of the receiver and trustee may be agreed upon and paid by consent of all parties.

§ 2118. Receiver's Compensation.—The receiver, of course, is allowed compensation.⁸⁰

But where he has been negligent in the performance of his duty, the court may deny him commissions.

In re Schoenfeld, 25 A. B. R. 748, 183 Fed. 219 (C. C. A. Pa.): "Where a receiver or trustee has been negligent in the performance of his duty, the court may, in a proper case, without the filing of exceptions, deny him any commissions."

Nor will the receiver be allowed compensation for worthless and unnecessary services.⁸¹

§ 2119. Receiver's Maximum Rate of Compensation Same as Trustee's.—By the Amendment of 1910 the receiver has been placed on the same plane with the trustee and his compensation is governed by the same maximum rate, and in general, by the same rules.⁸²

79. Bankr. Act, § 52b: "Marshals shall respectively receive from the estate where an adjudication in bankruptcy is made, except as herein otherwise provided, for the performance of their services in the proceedings in bankruptcy, the same fees, and account for them in the same way, as they are entitled to receive for the performance of the same or similar services in other cases in accordance with laws now in force, or such as may be hereafter enacted, fixing the compensation of marshals."

80. In re Scott, 3 A. B. R. 625, 99 Fed. 404 (D. C. N. Car.); In re Kirkpatrick, Rec'r, 17 A. B. R. 597, 148 Fed.

811 (C. C. A. Mich.). Instance, In re Martin-Borgeson Co., 18 A. B. R. 178, 151 Fed. 780 (D. C. N. Y.). Bankr. Act, § 48 (d) and (e), as amended in 1910.

81. In re Desrochers, 25 A. B. R. 703, 183 Fed. 991 (D. C. N. Y.).

82. Bankr. Act, § 48 (d and e).

Rulings before Amendment of 1910.—Some courts held, though there was no express provision governing the amount of the receiver's compensation, that the maximum allowance, at any rate for conducting the business, was not to exceed that of the trustee. In re Richards, 11 A. B. R. 581, 127 Fed. 772 (D. C. Mass.); apparently Dunlop Hdw. Co. v. Huddleston, 21 A. B. R.

The receiver's compensation is not to be deducted from that of the trustee, but is in addition thereto.

[Before Amendment of 1910] In re Richards, 11 A. B. R. 581, 127 Fed. 772 (D. C. Mass.): "I think therefore, that the court is permitted to allow as maximum compensation to receivers who have carried on the business, the maximum compensation allowed to trustees by § 48; this receivers' allowance not necessarily to be deducted from the trustees' maximum, but in some cases reckoned in addition to the latter. Referees will understand that this is the maximum, not the minimum or the normal, compensation of receivers. Sometimes the receiver's duties are merely formal and so his compensation should be small. Sometimes he has so far settled the bankrupt's estate that the trustee's duties are little more than formal, and so the trustee's compensation should be small. In many cases the rule hitherto adopted by the referee may well be proper, but I do not think it is absolutely binding in all cases. Its universal adoption would so limit the compensation of receivers as to make a suitable appointment difficult in some cases. An efficient administration of the Bankrupt Act calls for a reasonable liberality in this matter. The opinion just expressed applies only to receivers who have carried on the business. The compensation allowable to other receivers is not here in question."

§ 2119¼. Compensation in Composition Cases.—By the Amendment of 1903 the trustee's compensation in composition cases was reduced to one-half of one per cent. upon the amounts disbursed to creditors. This provision was not changed by the Amendment of 1910, but was re-incorporated therein as the rule for compensation for both the trustee and receiver in composition cases, with an additional one-half of one per centum where he conducted the business.⁸³

721, 167 Fed. 433 (C. C. A. Ga.); In re Leonard, 24 A. B. R. 97, 177 Fed. 503; In re Cambridge, 14 A. B. R. 168, 136 Fed. 983 (D. C. Mass.). "The amendment [that of 1903] is intended to provide that receivers shall not be more highly paid than trustees. The receiver's maximum allowance, therefore, is that stated percentage upon disbursements which is fixed as the maximum compensation of the trustee." However, it was held in other cases that the receiver's compensation was to be simply whatever was found in the court's discretion to be reasonable. In re Scott, 3 A. B. R. 365, 99 Fed. 404 (D. C. N. Car.); inferentially, In re Sully, 13 A. B. R. 22, 142 Fed. 895 (D. C. N. Y., affirming 13 A. B. R. 783); instance, In re Kyte, 19 A. B. R. 768, 158 Fed. 121 (D. C. Pa.); instance, In re Hughes, 22 A. B. R. 303, 170 Fed. 809 (D. C. N. J.); In re Martin-Borgeson Co., 18 A. B. R. 178, 151 Fed. 780 (D. C. N. Y.): "From an examination of the bankruptcy law the question of compensation to receivers and their attorneys seems to be entirely with the discretion of the court." It was held before the Amendment of 1910 that it was left

at any rate to the discretion of the court for services other than those in conducting the business. In re Kirkpatrick, 17 A. B. R. 595, 148 Fed. 811. But even for conducting the business it was held to be discretionary in some cases. In re Shiebler & Co., 23 A. B. R. 162, 174 Fed. 336 (C. C. A. N. Y.); In re Falkenberg, 30 A. B. R. 718, 206 Fed. 835 (D. C. N. Mex.).

83. Bankr. Act as amended 1910, § 48a: "And in case of the confirmation of a composition after the trustee has qualified, the court may allow him, as compensation, not to exceed one-half of one per centum of the amount to be paid the creditors on such composition. * * * (d) Receivers or marshals appointed pursuant to § 2, subd. 3, of this act shall receive for their services, payable after they are rendered, compensation by way of commissions, etc. * * * Provided, That in case of the confirmation of a composition such commissions shall not exceed one-half of one per centum of the amount to be paid creditors on such compositions: * * * (e) Where the business is conducted by trustees, marshals, or receivers, as pro-

It was unfortunate that the Amendment of 1903 regulating compensation in composition cases was brought forward into the Amendment of 1910. Whilst, no doubt, the amount of work for a receiver or trustee in composition cases is probably not as great as where the estate is administered throughout in bankruptcy, yet the compensation of one-half of one per cent. in composition cases is altogether too small. The hardship is somewhat alleviated by the practice in some districts of appointing the receiver or trustee in composition cases as the distributing agent to distribute the "consideration" to be paid to creditors for the ransoming of the bankrupt estate. The maximum rates of compensation limited by § 48 were meant for the protection of the bankrupt estate and not for that of an outside redemption fund and the statute only relates to the compensation of the officers for administering the bankrupt estate. The "consideration" deposited by or for the bankrupt in composition cases is for the purpose of redeeming the estate (rather than for administering it) and manifestly is an entirely different fund, in theory at least, from the bankrupt estate itself, and creditors are not interested in what allowance may be made out of that fund to the distributing agent for his care in making the distribution of the consideration to creditors. The "consideration" is to be "distributed as the court may direct" and the distributing agent who performs the distribution may be compensated as the court deems suitable. It is only upon the supposition that the court will appoint the receiver or trustee in composition cases distributing agent that the allowance of one-half of one per cent, respectively, for the receiver's and trustee's services before the composition is endurable.

§ 2119½. **Receiver as "Mere Custodian."**—The amendment of 1910 provides that where the receiver or marshal acts as a "mere custodian" and "does not carry on the business" he is not to receive more than two per cent on the first \$1,000 or less and one-half of one per cent on all above \$1,000. The insertion of this proviso has produced some ambiguity, especially from its unfortunate wording—"And does not carry on the business." This latter clause might seem to imply that all cases where the receiver does not carry on the business would be cases where he would be merely a custodian. But this is not the meaning of the proviso. The proviso is meant to cover cases where the receiver has acted as a temporary guard, locking up the establishment and performing no administrative duties whatever in relation thereto,⁸⁴ a mere "key turner," so to speak. Wherever the receiver does more than act as a mere key turner or guard the court may allow him the compensation allowed in the earlier clauses

vided in clause five of section two of this act, the court may allow such officers additional compensation for such services by way of commissions upon the moneys disbursed or turned over to any person, including lienholders, etc. * * * Provided, That in case

of the confirmation of a composition such commissions shall not exceed one-half of one per centum of the amount to be paid creditors on such composition."

⁸⁴. In re Griesheimer, 31 A. B. R. 567, 209 Fed. 134 (C. C. A. Cal.).

of § 48-d. Such must be the necessary construction, otherwise the provision with regard to his compensation would be rendered meaningless.⁸⁵

Compare, *In re Knosher & Co.*, 28 A. B. R. 747, 197 Fed. 136 (C. C. A. Wash.): "We do not think that the continuing of the business of the bankrupt by his employees for the remainder of one day constituted the carrying on of the business by the receiver within the meaning of the statute. On the other hand, we think the receiver was something more than a custodian, and that he was entitled to compensation as receiver under § 48d."

§ 2119³. Notice of Application for Compensation.—By the Amendment of 1910 to § 48 (d) and (e), it is prescribed that, except as to the allowance of the trustee's ordinary compensation, notice of the application for compensation of the receiver and trustee must be given to all creditors, stating the amount applied for.^{85a}

§ 2120. Appeal and Review of Expenses, and Costs of Administration.—The question of the appeal and review of costs of administration is taken up in detail, later, under the general subject of Appeal and Error.⁸⁶

SUBDIVISION "E."

FEES OF APPRAISERS, WITNESSES AND MARSHAL.

§ 2121. Appraisers' Fees.—Appraisers may be allowed compensation out of the estate. Their compensation must be reasonable, and, in its allowance, the manifest spirit of economy in which the Bankrupt Act was framed must be observed. Minute calculations as to the value of each article in detail is not required⁸⁷ and time thus spent by appraisers may not be liberally compensated for.⁸⁸

In re Kyte, 19 A. B. R. 768, 158 Fed. 121 (D. C. Pa.): "The main purpose of an appraisement is simply to get a general idea of the extent of the estate,

⁸⁵. *In re Ginsburg*, 31 A. B. R. 240, 208 Fed. 160 (D. C. Tenn.).

^{85a}. See Bankr. Act, § 48 b and e: "Provided further, that before the allowance of compensation, notice of application therefor, specifying the amount asked, shall be given to creditors in the manner indicated in section fifty-eight of this act." See also, ante, § 565³/₄.

See Report No. 691 of the Senate Judiciary Committee of the 61st Congress, Second Session: "Of course, the rates of commission prescribed are maximum limitations. Less, but not more, may be allowed; and it is hoped the courts will exercise their discretion still in allowing less amounts where proper. It is further to be observed that creditors are to be given notice of all applications for allowance, and thus there is afforded an

additional safeguard. The changes proposed by sections 1 and 9 of the amendatory bill will then, it is thought, tend to prevent extravagance in the administration of insolvent estates and to remove the temptation which now exists toward the creation of prolonged receiverships, and will also tend to put the administration of bankrupt estates promptly into the hands of trustees elected by the creditors, in accordance with the actual design of the framers of the Bankruptcy Act, rather than in the hands of receivers appointed by the courts."

⁸⁶. See post, § 2839, et seq.

⁸⁷. *In re Gordon Supply & Mfg. Co.*, 13 A. B. R. 352, 133 Fed. 798 (D. C. Pa.).

⁸⁸. *In re Gordon Supply & Mfg. Co.*, 13 A. B. R. 352, 133 Fed. 798 (D. C. Pa.).

so as to charge the party in whose custody it is with its value, and at the same time enable all concerned the better to keep track of it. Incidentally it may serve as a guide also to prospective buyers, but it is not to be independently undertaken with that in view, and except for this purpose it is difficult to see what object was gained in going over the same goods a second time."

In *re Fidler & Son*, 23 A. B. R. 16, 172 Fed. 635 (D. C. Pa.): "The expense of taking the inventory is outrageous, each appraiser receiving \$40. This is an extravagance which cannot be countenanced. The cost of appraisements is getting to be an abuse, which if not taken in hand by the courts, will lead to radical action by Congress. A per diem fee of \$5 is all that is allowed in this district, and it must be an extraordinary case where over two or three days are necessary. If there is occasion for anything more than that, the trustee must justify it."

Appraisers will not be allowed compensation for worthless and unnecessary services, although rendered at the request of a receiver.⁸⁹

§ 2122. Witness Fees and Mileage.—Witness fees and mileage are allowable out of the estate as part of the costs of administration.⁹⁰

§ 2123. Bankrupt Not Entitled to Witness Fees.—The bankrupt is not entitled to witness fees. His rights in this regard being provided for by § 7 (a) giving him reimbursement for certain expenses, it will be presumed that this provision is exclusive of compensation or other reimbursement.⁹¹

§ 2124. But to Reimbursement of Actual Expenses Where Attending.—The bankrupt, however, is entitled to reimbursement out of the estate for his actual expenses in attending the sittings of the bankruptcy court, when ordered to do so, at a place other than the city, town or village of his residence.⁹²

§ 2125. But None Where Voluntarily Removing Residence after Bankruptcy Instituted.—The bankrupt may not be allowed his expenses where he voluntarily removes his residence to another place or into another district after he has commenced proceedings.⁹³ Otherwise a bankrupt could remove his home to distant parts and then elude examination unless his necessary expenses were paid to him; and thus could so annoy and over-

^{89.} In *re Desrochers*, 25 A. B. R. 703, 183 Fed. 991 (D. C. N. Y.).

^{90.} As to witness fees allowed as costs recoverable by alleged bankrupt upon dismissal of petition against him where property was seized, see, *Hoffschlaeger Co. v. Young Nap*, 12 A. B. R. 526 (D. C. Hawaii).

^{91.} See ante, § 1577.

^{92.} Bankr. Act, § 7 (a).

The bankrupt can not be required to attend a meeting of his creditors, or at

or for an examination at a place more than one hundred and fifty miles distant from his home or principal place of business, or to examine claims, except when presented to him, unless ordered by the court or the judge thereof for cause shown. Bankr. Act, § 7 (a) (9).

See ante, "Discovery," § 1577.

^{93.} In *re Groves*, 6 A. B. R. 732 (Ref. Ohio, affirmed by D. C.), quoted, § 1578.

burden his creditors as to frustrate them entirely in making a proper discovery of the assets they are entitled to.

§ 2126. Whether Officers and Directors of Bankrupt Corporation Entitled to Witness Fees.—It is a query whether officers and directors of a bankrupt corporation are entitled to witness fees when examined. There is considerable force in the contention that they are not so entitled; for they are to be considered "the bankrupt" in similar relations of duty, such as that of preparing schedules, etc.⁹⁴

§ 2127. Witness Fees for Attendance without Subpœna Equally Allowable.—Fees paid witnesses attending without being subpœnaed are to be allowed as costs.⁹⁵

§ 2128. Amount of Witness Fees.—Witnesses in bankruptcy are entitled to the usual fees and mileage allowed in federal courts, namely, \$1.50 per diem and five cents per mile each way.

No mileage may be charged for the travel of witnesses, in the absence of an affidavit showing their residence or place of business, or the distance necessarily traveled.

§ 2129. Marshal's Fees.—The marshal is entitled to his customary fees.⁹⁶

Section 829, Rev. Stat., U. S., prescribes the marshal's fees. The marshal's fees, as distinguished from his compensation as custodian of the property, and in the conducting of the business, are not affected by the Amendment of 1910, that amendment referring simply to allowances out of the assets for caring for them, § 48d referring to the marshal's compensation when appointed under § 2 (3), and § 48e referring to his compensation for conducting the business under § 2 (5). His fees for service of papers are prescribed by § 52b, taken in connection with § 829 of the Revised Statutes of the United States.

§ 2130. Marshal May Demand Indemnity.—The marshal is entitled to demand indemnity.⁹⁷

94. Impliedly, Bankr. Act, § 1 (a) (19): "'Persons' shall include corporations, except where otherwise specified, and officers, partnerships and women, and when used with reference to the commission of acts which are herein forbidden shall include persons who are participants in the forbidden acts, and the agents, officers, and members of the board of directors or trustees, or other similar controlling bodies of corporations."

Compare, analogously, *In re Alphin & Lake Cotton Co.*, 12 A. B. R. 653, 128 Fed. 834 (D. C. Ark.).

95. *Hoffschlaeger Co. v. Young Nap*, 12 A. B. R. 526 (D. C. Hawaii).

96. Bankr. Act, § 52 (b): "Marshals shall respectively receive from the estate where an adjudication in bankruptcy is made, except as herein otherwise provided, for the performance of their service in proceedings in bankruptcy, the same fees, and account for them in the same way, as they are entitled to receive for the performance of the same or similar services in other cases in accordance with laws now in force, or such as may be hereafter enacted, fixing the compensation of marshal."

97. Gen. Order X.

§ 2131. May Charge Reasonable Fee for Services on Petition to Show Cause.—The marshal may charge a reasonable fee for service of a petition accompanying a show cause order, although it be not specifically mentioned in § 829, U. S. Rev. Stats.⁹⁸

§ 2132. Marshal and Receiver Entitled to Compensation, Besides Expenses, on Seizures under § 2 (3).—The marshal is entitled to compensation, in addition to his disbursements, when he takes possession of the goods of the bankrupt on the order of the bankruptcy court under § 2 (3).⁹⁹

In *re Adams Sartorial Co.*, 4 A. B. R. 107, 101 Fed. 215 (D. C. Colo.): "The question arises under the third clause of § 2 of the Bankruptcy Act, by which the court has authority to appoint a receiver, or the marshal, upon application of parties in interest, in cases where it shall appear to be necessary for the preservation of the estate, to take charge of the property of the bankrupt, and after the filing of the petition, and until it is dismissed or the trustee is qualified. If a receiver should be appointed under this clause of the act, there would be no question as to his right to compensation for his services, and I do not perceive that it can make any difference if the marshal shall act in that capacity. The circumstances that he receives a salary for all services performed by him is not controlling. The referee seems to have assumed that, because he did not personally get the compensation allowed, therefore it was not intended that he should have it. That is not the fact. The marshal does get personal compensation for all services rendered by him, in the way of salary; and fees which were allowed him as compensation before the act fixing a salary are still collected in suits of all kinds, as a fund out of which salaries shall be paid. So that the fact that there is a salary is a matter of no weight. I think the marshal is as much entitled to pay for his services in keeping the property as a receiver would be if a receiver had been appointed. The pay ought to be in amount such as the act requires in respect to other services which may be rendered by officers, and the fees allowed to all officers under this act are small—so small that there is a good deal of grumbling about them—but still the officers go on and accept what they can get."

Amendment of 1910.—The compensation of the marshal, receiver and trustee, as distinguished from their expenses, allowable out of the assets administered, for making seizures under Bankr. Act, § 2 (3), is established by the Amendment of 1910 upon a commission basis, upon moneys disbursed by them or afterwards realized by the trustee from

⁹⁸. In *re Damon*, 5 A. B. R. 133, 104 Fed. 775 (D. C. N. Y.). Compare, to same effect, inferentially, In *re Scott*, 3 A. B. R. 625, 99 Fed. 404 (D. C. N. Car.).

⁹⁹. It was held, before the Amendment of 1910, that there was no fixed rule for his compensation for making

such seizures. In *re Scott*, 3 A. B. R. 625, 99 Fed. 404 (D. C. N. Car.).

It was likewise held before the Amendment of 1910 that the receiver was entitled to what compensation the court might deem reasonable for making such seizures. In *re Kirkpatrick, Receiver*, 17 A. B. R. 594, 148 Fed. 811 (C. C. A. Mich.).

property turned over in specie to him.¹

1. Bankr. Act, § 48 (d): "(d) Receivers or marshals appointed pursuant to section two, subdivision three, of this act shall receive for their services, payable after they are rendered, compensation by way of commissions upon the moneys disbursed or turned over to any person, including lien holders, by them, and also upon the moneys turned over by them or afterwards realized by the trustees from property turned over in kind by them to the trustees, as the court may allow, not to exceed six per centum on the first five hundred dollars or less, four per centum on moneys in excess of five hundred dollars and less than one thousand five hundred dollars, two per centum on moneys in excess of one thousand five hundred dollars and less than ten thousand dollars, and one per centum on moneys in excess of ten thousand dollars: Provided, That in case of the confirmation of a composition such commissions shall not exceed one-half of one per centum of the amount to be paid creditors on such compositions: Provided further, That when the receiver or marshal acts as a mere custodian

and does not carry on the business of the bankrupt as provided in clause five of section two of this act, he shall not receive nor be allowed in any form or guise more than two per centum on the first thousand dollars or less, and one-half of one per centum on all above one thousand dollars on moneys disbursed by him or turned over by him to the trustee and on moneys subsequently realized from property turned over by him in kind to the trustee: Provided further, That before the allowance of compensation notice of application therefor, specifying the amount asked, shall be given to creditors in the manner indicated in section fifty-eight of this act."

See also, ante, § 2115, et seq. Where no adjudication results, the compensation, so far as allowable out of the assets administered, cannot exceed the maximum commissions established by the statute in § 48; although as to any compensation taxed as part of the costs to be paid by petitioning creditors by way of a money judgment against them, neither the rate of § 48 nor the prohibitions of § 72 are applicable.

CHAPTER XLI.

DISTRIBUTION TO CREDITORS.

Synopsis of Chapter.

- § 2133. Distribution.
- § 2134. Order of Priority in Distribution Prescribed by Act.
- § 2134½. Law in Force at Date of Adjudication Controls.
- § 2135. Priority Not Lost by Taking Judgment or Note; nor by Assignment of Claim.
- § 2136. Not Lost Where Claim Also a Secured Debt.
- § 2137. Mere Judgments Not Entitled to Priority as Such.
- § 2138. "Proof" of Priority Claim Requisite, Except for Taxes, etc.
- § 2139. No Special Form of Proof nor Assertion of Demand Requisite.
- § 2140. "Dividends" on Priority Claims Where Funds Insufficient.

DIVISION 1.

- § 2141. Taxes.
- § 2142. Assessed before Bankruptcy Though Not Payable until after Adjudication, Nevertheless "Due and Owing."
- § 2143. Back Taxes, Omitted, to Be Paid.
- § 2144. Delinquent Penalties and Interest.
- § 2145. Taxes to Be Paid Whether Property Comes into Trustee's Hands or Not.
- § 2146. Taxes on Exempt Property to Be Paid.
- § 2147. Taxes to Be Paid Out of General Fund Though Only One Benefited Is Mortgagee, Purchaser, etc.
- § 2148. But Such Absolute Priority Belongs Solely to State, Municipality, etc., Not to One Who Has Paid or Holds Tax Title.
- § 2149. "Subrogation" to Tax Lien Sometimes Proper.
- § 2150. Must Be Owing by Bankrupt and Assessed against Him.
- § 2151. Firm Taxes in Individual Bankruptcies.
- § 2152. Funds in Hands of Trustee Taxable, Where Taxable if Similarly Sequestered by State Legal Proceedings.
- § 2152½. Broad Use of Term "Tax" in Bankruptcy.
- § 2153. "Tax" Includes Assessment for Local Improvements.
- § 2154. Nature of Tax, Whether License, Penalty or Tax, Generally Determined by State Law.
- § 2155. But Not Always.
- § 2156. Thus, Franchise Tax.
- § 2157. But Bankruptcy Court, Forum as to Amount and Legality of Tax.
- § 2158. And Decision of State Board of Assessment Not "Res Judicata."
- § 2159. Nor Is Failure to Pursue Statutory Appeal or Abatement Fatal.
- § 2160. Whether Taxes "Provable" Debts.
- § 2161. No Formal "Proof" Required: Trustee Must Search for Taxes.
- § 2162. Year's Limitation for "Proof" Not Applicable to Taxes.
- § 2163. Tax Not Such "Secured" Claim as Requires Exhaustion of Security.

DIVISION 2.

- § 2164. "Wages of Workmen, Clerks, Salesmen and Servants."
- § 2165. Must Be "Wages" and Be "Due" and "Earned."
- § 2166. Thus, No Priority for Damages for Breach of Contract of Employment.

- § 2167. Only "Workmen," "Clerks," "Salesmen" or "Servants" Entitled.
- § 2168. Relationship between Parties Governs and Not Solely Kind of Work.
- § 2169. "Workmen," "Clerk," "Salesman" and "Servant" to Be Given Ordinary, Popular Meaning.
- § 2170. "Traveling or City Salesman" also Entitled to Priority.
- § 2170½. Though Paid by Commissions.
- § 2171. Definition of "Wage Earner" in §§ 1 and 4 Not Criterion Here.
- § 2172. Thus, Independent Contractors Not Entitled.
- § 2173. Exclusive Employment by One Person Not Requisite.
- § 2174. But Employment by Several Tends to Show Independent Contractor.
- § 2175. "Piece Workers" May Be Entitled.
- § 2176. Idea of Subordination Implied.
- § 2177. Correlative Obligation to Serve Implied.
- § 2178. Must Be Performed within Three Months before Bankruptcy.
- § 2179. Whether May Be for Services Covering Longer Period if Priority Claimed Not under § 64 (b) (4) but under § 64 (b) (5).
- § 2179½. Application of Payments to Wages Earned before Three Months.
- § 2180. Not to Exceed "Three Hundred Dollars."
- § 2181. But Perhaps for More if Priority Claimed Not under § 64 (b) (4) but under § 64 (b) (5).
- § 2182. Reducing Claim to Judgment, Not Such Merger as to Lose Priority.
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- § 2262 $\frac{1}{4}$. Claim of Bankrupt Partnership against Its Bankrupt Member—Not to Share *Pari Passu* with Individual Creditors.
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SUBDIVISION "A."

- § 2277. Subrogation by Assignment of Claims after Bankruptcy.

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- § 2280. Subrogation of Sureties for Bankrupt to Creditors' Rights and of Creditors to Indemnity Given Sureties.
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- § 2286. Form of Trustee's Reports.
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- § 2294 $\frac{1}{4}$. And to Be Verified.
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§ 2133. **Distribution.**—In the orderly development of the treatise, after consideration of the subjects of the separation of the assets belonging to the creditors from those belonging to others, and the collecting and converting of the same into money, and the payment of the costs and expenses of administration, naturally the subject is reached of the distribution of the remaining proceeds among the creditors. This end, indeed, is precisely the goal towards which the bankruptcy proceedings have been directed in behalf of creditors.

A distinct purpose of the bankruptcy act is to subject the administration of the estates of bankrupts to the control of tribunals clothed with authority, and charged with the duty of proceeding to final settlement and distribution in a summary way, as are the courts of bankruptcy; and creditors are not only entitled to have this jurisdiction exercised, but they may justly complain where the administration of bankrupt estates, or any part thereof, is attempted by any other tribunal, even though it be with leave from the bankruptcy court.¹

§ 2134. **Order of Priority in Distribution Prescribed by Act.**—The Bankruptcy Act prescribes a certain order of priority in the payment of creditors out of the net amount of the fund left after separation of the property belonging to the estate from that belonging to adverse claimants,

1. U. S. *Fidelity v. Bray*, 225 U. S. 505, 28 A. B. R. 207.

secured creditors² and the bankrupt, and after the payment of the costs and expenses of administration.³

The word "preference" is frequently used when "priority" is meant. "Preference," in bankruptcy law, has a distinct meaning and the meaning is invidious.⁴

The order of priority is, in general, first, taxes; second, certain wages of workmen, clerks and servants; third, priorities given by state and federal laws; and lastly, dividends to general creditors.

§ 2134½. Law in Force at Date of Adjudication Controls.—The statute in force at the date of adjudication controls the right of priority throughout the case.⁵

§ 2135. Priority Not Lost by Taking Judgment or Note; nor by Assignment of Claim.—Priority is not, in general, lost by taking judgment, by acceptance of a note, or by assignment of the claim. Thus, it is not lost by taking judgment, whether the priority be one created by the bankruptcy act,⁶ or be a state priority adopted in bankruptcy under § 64 (b) (5), if not thereby forfeited by state law.⁷ It is not lost by the acceptance of a note.

In re Worcester County, 4 A. B. R. 496, 102 Fed. 808 (C. C. A. Mass.): "Taking a note does not discharge an original debt which has any privileges, and either might be proved."

Nor by the assignment of the claim,⁸ at any rate not where the priority has become fixed before the assignment; nor even where the assignment occurred before the commencement of the bankruptcy proceedings.⁹

2. Contra, holding, but erroneously, that an otherwise valid chattel mortgage lien was displaced by priority claims under the Bankruptcy Act. In re McDavid Lumber Co., 27 A. B. R. 39, 190 Fed. 97 (D. C. Fla.). Compare, § 2186.

3. *Smith v. Motley*, 17 A. B. R. 865, 150 Fed. 266 (C. C. A. Ohio). See, in general, Bankr. Act, § 64; also inferentially, *Martin v. Orgain*, 23 A. B. R. 454, 174 Fed. 772 (C. C. A. Tex.).

[So much so that the Bankruptcy Act's priority to workmen held to override lien given by State Law to a chattel mortgage, although without bankruptcy the lien would be good]. In re McDavid Lumber Co., 27 A. B. R. 39, 190 Fed. 97 (D. C. Florida).

Guarantee Title and Trust Co. v. Title Guarantee and Surety Co., 224 U. S. 152, 27 A. B. R. 873; In re Yoke Vitriified Brick Co., 25 A. B. R. 18, 180 Fed. 235 (D. C. Kans.).

4. *Smith v. Motley*, 17 A. B. R. 865, 150 Fed. 266 (C. C. A. Ohio): "* * *

But even in proceedings in bankruptcy priorities or 'preferences,' as they are sometimes called, when 'priorities' are meant * * *"

5. In re Photo Engraving Co., 19 A. B. R. 94, 155 Fed. 684 (D. C. N. Y.).

6. In re Anson, 4 A. B. R. 231, 101 Fed. 698 (D. C. Calif.). Compare, In re McBryde, 3 A. B. R. 729, 99 Fed. 686 (D. C. N. Car.). Compare, In re Blackstaff Engr. Co., 29 A. B. R. 663, 200 Fed. 1019 (D. C. Ga.).

7. Compare, In re Johnson, footnote to 4 A. B. R. 231 (D. C. Calif.).

8. In re Worcester County, 4 A. B. R. 496, 102 Fed. 808 (C. C. A. Mass.); In re Harmon, 11 A. B. R. 64, 128 Fed. 170 (D. C. W. Va.); (1867) In re Brown, Fed. Cas. 1,974; contra, In re Westlund, 3 A. B. R. 646, 99 Fed. 399 (D. C. Minn.). Also contra, obiter, In re North Carolina Car Co., 11 A. B. R. 488, 127 Fed. 178 (D. C. N. Car.).

9. Shropshire, Woodliff & Co. v. Bush, 17 A. B. R. 78, 204 U. S. 186.

§ 2136. **Not Lost Where Claim Also a Secured Debt.**—The priority is not lost where the claim is also a secured debt.¹⁰ The creditor simply has two sources of payment, his security and his priority. It is even doubtful whether there exists any right to require the exhaustion of the security first.¹¹

§ 2137. **Mere Judgments Not Entitled to Priority as Such.**—A merely personal judgment, the claim on which it is founded not being entitled to priority, is not entitled as such to priority of payment out of the general funds, nor is it entitled to payment from the proceeds of any particular part of the property, unless it is a lien thereon under the state law.¹²

§ 2138. **"Proof" of Priority Claim Requisite, Except for Taxes, etc.**—Due proofs of claim are requisite for priority claims, precisely as for other claims of creditors. They are none the less "provable" debts because entitled to priority of payment. Thus, claims for rent must be proved where certain priority is given to the landlord by state law. Taxes are provable debts and may be "proved" even though in general they must be taken care of without any prerequisite filing of claims by the sovereign.¹³

§ 2139. **No Special Form of Proof nor Assertion of Demand Requisite.**—No special form of proof is prescribed for priority claims; nor is it requisite that the claimant assert his right to the priority by formal demand in the affidavit.

In re Worcester Co., 4 A. B. R. 502, 102 Fed. 808 (C. C. A. Mass.): "Nothing is found in the orders giving any special direction with reference to the manner of proving claims in connection with which a priority is asserted. Neither do the prescribed forms for proofs of debts contain anything of that character, although the form of the proof of a secured debt requires that it shall enumerate the securities held by the creditor. Neither is there anything in the statute giving any direction as to the method of proving a debt in reference to a priority. The topic is covered by § 57 (30 Stat. 560). The first paragraph of that section ("a") gives detailed directions for the proof, but it omits any reference to the matter of priority, although it is express about proofs by creditors holding securities. Paragraph "e" provides that the claims of secured creditors and of those who have priorities may be allowed, in order to enable such creditors to participate at meetings held prior to the determination of the value of their securities or priorities, but they are thus to be allowed for such sums only as to the court seems to be owing over and above the value of their securities or priority. This, however, concerns only the preliminary determination in a preliminary way of the franchise rights of creditors. * * * There is nothing in this section (64) to indicate that the question of priority is essentially involved in the mere matter of proving a debt, or even that a claim to priority should appear in the formal proof."

10. *Chattanooga v. Hill*, 15 A. B. R. 197, 139 Fed. 600 (C. C. A. Tenn.).

11. But compare, *In re Barr Pumping Engine Co.*, 11 A. B. R. 313 (Ref. Pa.).

12. *In re Wood*, 2 A. B. R. 695, 95 Fed. 946 (D. C. N. Car.).

13. See, as to taxes, post, § 2161. See, as to other claims of the government, post, § 2191.

However, the affidavit for proof of debt should, in practice, contain allegations sufficient to show the debt is one of those enumerated in § 64 as entitled to priority and such affidavit should be sufficient where no objection is made to establish the priority.

It is not necessary that the right of priority be asserted before the expiration of the year limited for proving claims, if the debt itself be proved in time.

In *re Ashland Steel Co.*, 21 A. B. R. 834, 168 Fed. 679 (D. C. Ky.): "The privilege was not a detached right, which could only be fastened by special proceedings taken to enforce it, as by an attachment or an execution or the enforcement of a mechanic's lien. It needed only to be proved, when the time should arrive for distributing the assets. * * * We think that, the substantive claims having been proven within the time allowed by the act, it was within the power of the court to allow the claims priority, and give them the preference to which by law they were entitled, notwithstanding no definite claim of the kind had been made during the year. It was not the allowance of a new claim, as counsel for petitioners insist, but the giving full scope to one already proved. It was essentially the ascertainment of its rank to be regarded in the distribution of the assets. The word 'claim,' in § 57n we should suppose, refers to the substance of the obligation, rather than to any mere attribute of it."

And the fact that the priority claimant inadvertently participated in the election of the trustee, as if his claim were not entitled to priority, will not constitute an estoppel nor a waiver of the priority.¹⁴

§ 2140. "Dividends" on Priority Claims Where Funds Insufficient.—Of course, if there is not enough to pay any particular class of the priority claimants in full, a dividend of a per cent. should be declared to such priority claimants. There can be a dividend to priority creditors precisely as well as to general creditors.¹⁵

DIVISION 1.

TAXES.

§ 2141. Taxes.—The first creditor to be taken care of, is, of course, the state.

In *re Yoke Vitriified Brick Co.*, 25 A. B. R. 18, 180 Fed. 235 (D. C. Kan.): "* * * anything inhering in the general principles of equity or the law, such, for example, as the duty of the property to contribute its just proportion of the expense of government, or to pay its pro rata share of the expenses incurred in the preservation of the estate, and such like matters, remain still enforceable against the estate, although covered by fixed liens and against the consent of the holder of such liens, for such expenses are incurred for the protection of the lienholder and are enforceable for that reason and not because embodied in the act."

¹⁴ In *re Ashland Steel Co.*, 21 A. B. R. 834, 168 Fed. 679 (C. C. A. Ky.). See also, ante, § 576.

¹⁵ In *re Muhlhauser*, 9 A. B. R. 81 (Ref. Ohio).

The act prescribes that the court shall order the trustee to pay all taxes legally due and owing by the bankrupt to the United States, state, county, district or municipality, in advance of the payment of dividends to creditors.¹⁶

In *re Prince & Walter*, 12 A. B. R. 678, 131 Fed. 546 (D. C. Pa.): "Taxes, as a class, are thus put at the head of everything—even above the expense of preserving the estate, or the cost of administering it."

It is incorrect to say, as was said in *In re Veitch*, 4 A. B. R. 112 (D. C. Conn.), that taxes come under § 64 (b) (5) in the order of priority as being "debts owing to any person who by the laws of the State or United States is entitled to priority."¹⁷

On the contrary, § 64 (a) specifies a distinct order of priority. That section of the statute would be deprived of all significance if taxes were comprehended within § 64 (b) (5). Moreover, the other paragraph of § 64, paragraph (b), refers to the order of priority "except as herein otherwise provided," clearly indicating that the only remaining paragraph "herein" was meant to prescribe a priority.¹⁸

Again, taxes from their nature ought to come next to costs in the order of priority, for without taxes the general government would fail; as, also without costs the particular protection of the state in the immediate property concerned could not be afforded. The state must not be delayed nor hindered in its collection of taxes and it is this urgency that lies at the basis of the priority given to taxes.¹⁹

City of Waco v. Bryan, 11 A. B. R. 481, 127 Fed. 79 (C. C. A. Tex.): "The sovereign cannot be hindered or embarrassed or postponed in the collection of his revenues. This policy was recognized in all the bankruptcy laws heretofore passed. Section 62 of the Bankruptcy Act of April 4, 1800, ch. 19, 2 Stat. 36, provides that 'nothing contained in this law shall in any manner affect the right

16. The Act of 1898 differs widely from the Act of 1867 in relation to taxes: *State of N. J. v. Anderson*, 17 A. B. R. 67, 203 U. S. 483.

Bankr. Act, § 64 (a). *State of N. J. v. Anderson*, 17 A. B. R. 65, 203 U. S. 483; *City of Waco v. Bryan*, 11 A. B. R. 481, 127 Fed. 79 (C. C. A. Tex.); *Chattanooga v. Hill*, 15 A. B. R. 195, 139 Fed. 600 (C. C. A. Tenn.); *Cooper Grocery Co. v. Bryan*, 11 A. B. R. 734, 127 Fed. 815 (C. C. A. Tex.); *In re Harvey*, 10 A. B. R. 567, 122 Fed. 745 (D. C. Pa.); *In re Flynn*, 13 A. B. R. 720, 134 Fed. 145 (D. C. Mass.); *In re Stalker*, 10 A. B. R. 713, 123 Fed. 961 (D. C. N. Y.); *In re Tilden*, 1 A. B. R. 301, 91 Fed. 501 (D. C. Iowa); *In re Conhaim*, 4 A. B. R. 58, 100 Fed. 268 (D. C. Wash.); *obiter*, *Sellers v. Bell*, 2 A. B. R. 542, 94 Fed. 801 (C. C. A. Ala.); *In re Hilbert*, 6 A. B. R. 714 (Ref. Penna.); *In re Cleanfast Hosiery Co.*, 4 A. B. R. 702 (Ref. N.

Y.); *In re Force*, 4 A. B. R. 117 (Ref. Mass.); *In re Wyoming Valley Ice Co.*, 16 A. B. R. 594, 145 Fed. 267 (D. C. Pa.); *In re Fisher & Co.*, 17 A. B. R. 412, 148 Fed. 907 (D. C. N. J.); *In re Lange Co.*, 20 A. B. R. 478, 159 Fed. 536 (D. C. Iowa); *In re Halsey Electric Generator Co.*, 23 A. B. R. 401, 175 Fed. 825 (D. C. N. J.); *In re Weissman*, 24 A. B. R. 150, 178 Fed. 115 (D. C. Conn.); *(State of) New Jersey v. Lowell*, 24 A. B. R. 562, 179 Fed. 321 (C. C. A. N. J., affirming *In re Halsey Electric Co.*, 23 A. B. R. 401, 175 Fed. 825), quoted post, this section.

17. *Chattanooga v. Hill*, 15 A. B. R. 195, 139 Fed. 600 (C. C. A. Tenn.).

18. Compare, *In re Cleanfast Hosiery Co.*, 4 A. B. R. 702 (Ref. N. Y.).

19. *In re Tilden*, 1 A. B. R. 301, 91 Fed. 501 (D. C. Iowa); *Chattanooga v. Hill*, 15 A. B. R. 195, 139 Fed. 600 (C. C. A. Tenn.).

of preference to prior satisfaction of debts due the United States.' Section 5 of the Act of August 19, 1841, ch. 9, 5 Stat. 444, gives priority to the United States (for all debts due by such bankrupt to the United States). Section 28 of the Act of March 3, 1867, ch. 176, 14 Stat. 530, gives priority, first, 'for the fees, costs and expenses of suit,' etc.; second, 'for all debts due the United States and all taxes and assessments under the laws thereof;' third, 'for all debts due to the State in which the proceedings in bankruptcy are pending, and all taxes and assessments made under the laws of such State.' The present Bankruptcy Law gives priority for all taxes legally due and owing by the bankrupt to the United States, the State, county, district or municipality, in advance of the payment of dividends to creditors. In short, it puts taxes due the State, counties and municipalities upon the same footing as taxes due the United States. On the plain construction of § 64a of the present law, and particularly in the light of past legislation on the subject, there is no room to hold that it makes any difference whatever, as to the right of priority, whether property on which taxes were assessed ever came into the hands of the trustee. The test is given in the statute: Are the taxes legally due and owing by the bankrupt to the United States, State, county, district or municipality claiming the same? If yea, they are entitled to be paid in advance of the payment of dividends to creditors, for thus saith the law."

In *re Stalker*, 10 A. B. R. 713, 123 Fed. 961 (D. C. N. Y.): "The significance of § 64 (a) * * * is that a claim for taxes is paramount to all other claims because of the pecuniary needs and requirements of the municipality."

In *re Halsey Electric Generator Co.*, 23 A. B. R. 401, 175 Fed. 825 (D. C. N. J.): "Keeping the legislative purpose of the Bankruptcy Act in mind, and viewing the language employed in the act in dealing with priorities, in the light of the foregoing suggestions, I am of the opinion that in the distribution of the assets of the bankrupt, the actual and necessary costs of preserving and administering the estate have priority over taxes."

The statute, in § 64 (b), provides, as the item entitled to the next place in the order of distribution after costs of administration, "wages due to workmen, clerks and servants;" nevertheless § 64 (a) provides that taxes are to be paid before creditors. So, the proper order of priority is for taxes next *after* costs of administration.²⁰

(State of) *New Jersey v. Lovell*, 24 A. B. R. 562, 179 Fed. 321 (C. C. A. N. J., affirming *In re Halsey Elect. Co.*, 23 A. B. R. 401, 175 Fed. 825): "Now, while the relative order in which subdivisions 'a' and 'b' are placed is not happy, and indeed tends to mislead, yet the general intent of the section is clear. In subdivision 'b' we find the general scheme of awarding priority in advance of dividend creditors. That subdivision makes provision for paying such costs, fees, and liens as are therein provided, and if there are no outstanding taxes the fund is then paid to creditors. But before paying creditors, subdivision 'a' intervenes and makes provision for what, if omitted, has often proved a hardship, if not indeed an abuse in the settlement of decedent and insolvent estates, viz., delay in payment of taxes. Tax collectors whose power to distrain

²⁰. Compare, *In re Oxley*, 30 A. B. R. 406, 204 Fed. 826 (D. C. Wash.).

Two cases, indeed [disapproved in *In re Halsey Electric Generator Co.*, 23 A. B. R. 401, 175 Fed. 825 (D. C. N. J.)], hold that taxes are to be paid before even costs of administration:

Obiter, *In re Prince & Walter*, 12 A. B. R. 678, 131 Fed. 546 (D. C. Pa.); *In re Weiss*, 20 A. B. R. 247, 159 Fed. 295 (D. C. N. Y.). But see *quære*, *Chattanooga v. Hill*, 15 A. B. R. 195, 139 Fed. 600 (C. C. A. Tenn.).

lapsed when the estate passed into the custody of the law, or who were left to come in as general creditors, were subjected to trying delays. Obviously subdivision 'a' meant that this delay should not occur, and therefore provided that, 'in advance of payment of dividends to creditors,' 'the court shall order the trustee to pay all taxes legally due and owing by the bankrupt to the United States, State, county, district or municipality,' and, to prevent delay from questions concerning such taxes, it provided, 'in case any question arises as to the amount or legality of any such tax, the same shall be heard and determined by the court.' And yet in case the court had to take testimony, or order a referee to determine the legality of such tax, the adjudged tax would, under the construction here contended for, absorb the whole fund and leave unpaid the agency by which its payment was effected. Now, whether the 'creditors' referred to in the phrase, 'in advance of the payment of dividends to creditors,' places the payment of taxes ahead of dividend creditors alone, or places it also ahead of those creditors who, under subdivisions 4 and 5 of clause 'b,' are paid in full, is a question not before us. It suffices to say that on the question that is before us, namely, whether the taxes of a State are, under clause 'a,' given priority over 'the actual and necessary cost of preserving the estate subsequent to the filing of the petition,' we are clear they are not."

In *re Halsey Electric Generator Co.*, 23 A. B. R. 401, 175 Fed. 825 (D. C. N. J.): "To my mind Congress has by apt words signified its intention to make taxes subordinate to the payment of the cost of preserving and administering a bankrupt's estate."

And it seems improper in theory and unnecessary from the point of view of statutory construction to place taxes in advance of costs of administration. Were they so placed, the administration of the estate might be completely blocked. The state is no more interested in the collection of taxes for the support of the government in its general functions than in the collection of the costs of its support in administering justice in the particular case immediately at hand—both taxes and costs are for the support of the government in the performance of its functions, and the particular support should have precedence over the general support, else the general support itself will fail.

Impliedly, (*State of*) *New Jersey v. Lovell*, 24 A. B. R. 562, 179 Fed. 321 (C. C. A. N. J., affirming *In re Halsey Elec. Gen. Co.*, 23 A. B. R. 401, 175 Fed. 825): "The question is of grave import, for it is clear that, if the administration of law is to be respected, a court, without power or means to pay for carrying out its orders, must refuse to make such orders; otherwise its helpless jurisdiction will incur merited contempt."

§ 2142. Assessed before Bankruptcy Though Not Payable until after Adjudication, Nevertheless "Due and Owing."—Taxes assessed against the bankrupt before bankruptcy, although not payable until after adjudication, are, nevertheless, "due and owing."²¹

²¹ In *re Flynn*, 13 A. B. R. 720, 134 Fed. 145 (D. C. Mass.); In *re Fisher & Co.*, 17 A. B. R. 412, 148 Fed. 907 (D. C. N. J.).

And the funds are taxable even if

the taxes are assessed after bankruptcy. In *re Fisher & Co.*, 17 A. B. R. 412, 148 Fed. 907 (D. C. N. J.). See also, post, § 2152.

§ 2143. Back Taxes, Omitted, to Be Paid.—Back taxes, omitted from the tax lists of previous years, are to be paid.²²

In re Conhaim, 4 A. B. R. 58, 100 Fed. 268 (D. C. Wash.): "The bankruptcy law very justly requires the trustee of a bankrupt estate to pay all taxes legally due and owing by the bankrupt, and the court will not favor any evasion of this law by giving a too liberal construction to its words * * * the omission of the property from the tax list for any year does not exempt it from taxation. On the contrary, it is the duty of the taxpayer to have the property listed by the tax collector and to pay the tax."

§ 2144. Delinquent Penalties and Interest.—The taxes are to be paid in full, including any penalties or interest for delinquency to the date of payment, the same as if the property were not in the hands of the court.²³

In re Kallak, 17 A. B. R. 414, 147 Fed. 276 (D. C. N. Dak.): "As other claims are not permitted to draw interest after the adjudication, it is therefore contended that the amount of the public demand for taxes is subject to the same restriction. The fact is, however, that under the Bankruptcy Law, § 64a, and other provisions dealing with the same subject, public taxes do not constitute a 'claim' in bankruptcy. It is not necessary for the public authorities to appear in a court of bankruptcy as ordinary claimants. They have no right in the administration as creditors and no voice in the selection of trustee, and the liability for taxes is in no way affected by the discharge of the bankrupt. On the other hand, the duty of the affirmative action rests upon the court of bankruptcy. It is the duty of the trustee to ascertain from the public records the amount due for taxes and bring the matter to the attention of the court, and thereupon it is the duty of the court to order their payment if there are sufficient funds in the estate for that purpose. There are two reasons why ordinary claims of creditors are not permitted to draw the interest subsequent to the adjudication; first, it is important that the proportionate interest of the several creditors in the estate be ascertained and fixed. If interest were to accrue, however, after the adjudication, the amount of the several claims would vary from time to time, according to their respective rates of interest and the proportionate share of the several creditors would be subject to constant readjustment. The second reason is the convenience of administration. If, at the declaration of every dividend, a new basis of apportionment were required, depending upon varying rates of interest, the administration of the estate would be seriously complicated. *Chemical National Bank v. Armstrong*, 59 Fed. 372, 379; *White v. Knox*, 111 U. S. 784. In the case of public taxes, neither of these reasons has any application because they do not share the estate with the claims of private creditors. On the contrary, § 64a expressly provides that before anything shall be paid to the creditors by way of dividends, all taxes owing by the bankrupt shall be fully discharged. The reason for claims becoming fixed at the date of the adjudication so that interest shall not subsequently accrue having no application to public taxes, the rule itself should not be applied in such cases."

²². Interest on taxes. In re Cosmopolitan Power Co., 14 A. B. R. 604, 137 Fed. 858 (C. C. A. Ills.); In re Weissman, 24 A. B. R. 150, 178 Fed. 115 (D. Conn.), quoted at § 2144.

²³. In re Cosmopolitan Power Co.,

14 A. B. R. 604, 137 Fed. 858 (C. C. A. Ills.); In re Schuyler & Co., 21 A. B. R. 428 (Ref. N. Y.). Contra, but point apparently not discussed in argument, In re Fisher & Co., 17 A. B. R. 413 (D. C. N. J.).

In *re Scheidt Bros.*, 23 A. B. R. 778, 177 Fed. 599 (D. C. Ohio): "No question as to taxes accruing and penalties imposed subsequent to the institution of the bankruptcy proceedings is involved. Whatever may be the rule elsewhere, in Ohio the penalty takes the place of interest. *Bridge Co. v. Mayer*, 31 Ohio St. 317, 328. Its allowance is intended to cover interest until the delinquent taxes are put into judgment (*Wheeling & Lake Erie Ry. Co. v. Wolfe*, 13 Ohio C. C. 374), or are paid voluntarily, or by special effort of the treasurer in person or by his agent—in some manner other than by process of law. The penalty, being treated as interest, is collectible as a part of the tax itself. 27 Am. & Eng. Ency. Law, 777, 778, 779. Under § 64 of the Bankruptcy Act the referee should have directed payment of both taxes and penalty."

Back taxes are to be paid, even though they absorb all, or a great part, of the assets; and even though the tax collectors have been negligent in making collection.

In *re Weissman*, 24 A. B. R. 150, 178 Fed. 115 (D. C. Conn.): "By this legislation Congress seems to have placed valid and subsisting taxes in a class by themselves and of the highest rank. The only possible question to be decided is whether the taxes, which the trustee has not been ordered to pay, were collectible from the bankrupt prior to adjudication. If they were legally due and owing at that time, they must be paid now. The referee seems to think that they were not, because the collectors had been guilty of laches in failing to collect sooner. Without explanation of the reasons for non-collection, it strikes one that the collectors have been disgracefully slack, but I cannot believe that in a suit against Weissman before bankruptcy such a defense would have been made, or, if it had been made, would have been seriously listened to by any court."

And taxes are not to lose their priority in favor of creditors whose assets have recently gone to swell the insolvent fund.²⁴

§ 2145. Taxes to Be Paid Whether Property Comes into Trustee's Hands or Not.—Taxes must be paid in advance of payments to other creditors, whether or not the property on which the taxes were assessed ever came into the hands of the trustee.²⁵

City of Waco v. Bryan, 11 A. B. R. 481, 127 Fed. 79 (C. C. A. Tex.): "This section is perfectly plain and seems to admit of very little, if any, construction. It is contended that it is inequitable for the bankrupt's estate to be compelled to pay, by priority, taxes originally levied on property which does not come into the hands of the trustee. To this it is sufficient answer to say that the priority to be given payment of claims against the bankrupt is within the control of the lawmaker, and is absolutely fixed by the statute, and the rule therein declared cannot be varied to meet ideas of what equity and good conscience may require. From the foundation of the government, it has been the policy

²⁴ In *re Weissman*, 24 A. B. R. 150, 178 Fed. 115 (D. C. Conn.), quoted, on another point, *supra*.

²⁵ In *re Prince & Walter*, 12 A. B. R. 678, 131 Fed. 546 (D. C. Pa.): This case goes even too far, holding, obiter, that taxes come ahead of costs of administration—a holding not required by

the wording of the statute nor by reason.

But a city is not entitled to a lien upon the assets for the amount of taxes assessed upon property that never came into its hands as trustee. *Waco v. Bryan*, 11 A. B. R. 481, 127 Fed. 79 (C. C. A. Tex.).

of the United States to exact priority in favor of the United States in all cases of insolvency. This policy is declared in § 3466 of the revised statutes, as follows:

“‘Priority Established. Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority hereby established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts, makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed or absent debtor are attached by process of law, as to cases in which an act of bankruptcy is committed.’”

And must be likewise paid though the property was abandoned by the trustee.²⁶

§ 2146. Taxes on Exempt Property to Be Paid.—Taxes on exempt property must be paid out of the estate.²⁷

In *re Tilden*, 1 A. B. R. 300, 91 Fed. 501 (D. C. Iowa): “There is no express exclusion of taxes against exempt property. The trustee is to pay ‘all taxes legally due and owing by the bankrupt.’ The creditors, however, plead what they term the ‘injustice’ of such a construction. The exempt property may have a large amount of taxes standing against it. The estate receives no benefit whatever from the exempt property. Where, as here, there is no question as to the property being exempt, the trustee, if he can in any wise be properly said to take such property under the adjudication of bankruptcy, takes it only for the purpose of at once passing it out as exempt property. So that, if received by him affected by the lien of the taxes, why should the trustee pass it back in a better condition than he received it? Wherein is his duty to lessen the general estate in his hands, by applying a part of the same to the removal of said tax liens, and thus lessening the amount otherwise distributable to the general creditors? If a mechanic’s lien, or other like lien, existed against said exempt property the general assets of the estate would not ordinarily be thus lessened to effect the removal of such lien. And the creditors call attention to this case as plainly showing the unjust result, as they term it, of the opposite construction of the statute. The amount in the hands of the trustee, if applied to pay these taxes on this exempt homestead, will be substantially exhausted, leaving barely sufficient to pay expenses of administration of the estate; and there seems much force in the argument. On the other hand, the bankrupt calls attention to the letter of the law—‘all taxes legally due and owing by the bankrupt,’—without any qualifying terms. And he properly insists that the burden is on the creditors to show why the statute does not intend what its terms plainly state. He also insists that this paragraph is a manifest recognition by Congress of the proposition that, whether any other creditor be paid or not, the government—national, State or municipal—is to have its taxes out of the estate. Again, the bankrupt might have paid these taxes at any time before filing his petition in bankruptcy. If, while on his way to the clerk’s office to file such petition, he had stopped at the taxpaying office, and there paid these taxes, and thereby reduced the general assets (actually turned into the estate by the amount of those

²⁶. Compare, obiter, in dissenting opinion, *City of Waco v. Bryan*, 11 A. B. R. 481, 127 Fed. 79 (C. C. A. Tex.).

²⁷. In *re Baker*, 1 A. B. R. 526 (Ref. Tex.). Compare, In *re Veitch*, 4 A. B. R. 112, 101 Fed. 251 (D. C. Conn.).

taxes), no one could have justly complained. He very effectively inquires why is the general creditor now injured by payment of these taxes out of the estate, if their payment, as above suggested, could not have been complained of by him?"

§ 2147. Taxes to Be Paid Out of General Fund Though Only One Benefited Is Mortgagee, Purchaser, etc.—Taxes upon property belonging to the estate will be ordered paid out of the general fund to the state or municipality or federal government as the case may be, although the only one benefited will be a mortgagee, or some particular creditor, or a purchaser of the assets. The taxes must be paid and paid out of the general fund, and be paid first before all other claims of creditors, regardless of benefit or lack of benefit, lien or lack of lien.²⁸

Chattanooga v. Hill, 15 A. B. R. 195, 139 Fed. 600 (C. C. A. Tenn.): "But, irrespective of the question of a lien, the taxes constituted a personal debt against the taxpayer which can be enforced by proceedings in personam. The Bankrupt Act says that 'all taxes legally due and owing by the bankrupt' shall be paid by the trustee 'in advance of the payment of dividends to creditors.' This does not say or mean that such payment shall be dependent upon the question as to whether they are a secured debt. * * * Congress evidently meant that the sovereign should neither be postponed nor delayed in the collection of taxes, and therefore provided that the trustee should pay all taxes due and owing by the bankrupt in advance of dividends. The bankrupt might have paid all taxes immediately prior to the filing of a petition by or against him. This would not have been a preference. The law means that the trustee shall do what the bankrupt might have done and what good citizenship required him to do. The opinions of the courts are not agreed about this matter, and there are holdings which limit this direction to pay 'all taxes due and owing by the bankrupt' to such taxes as constitute a lien upon the bankrupt's estate in the hands of the trustee and remit the sovereign to the enforcement of any lien which it may have against property which the trustee relinquished to the lien creditors."

But compare, *In re Stalker*, 10 A. B. R. 709, 123 Fed. 961 (D. C. N. Y.): "Some seemingly unjust features may be presented by the application of the stringent provisions of the Bankrupt Act referred to, but as the law is plain and singularly free from ambiguity, it is obvious that Congress intended that the statute should be strictly construed and applied, unless the facts disclose unjust or prejudicial results." In this case that portion of the taxes which was upon the real estate sold "subject to taxes" was excepted.

Compare apparently but not really contra, *In re Brinker*, 12 A. B. R. 122, 128 Fed. 634 (D. C. N. Y.): "Furthermore, none of the purchasers of the tax

²⁸ *In re City of Waco v. Bryan*, 11 A. B. R. 481, 127 Fed. 79 (C. C. A. Tex.), quoted supra, § 2145; *In re Prince & Walter*, 12 A. B. R. 679, 131 Fed. 546 (D. C. Pa.); *In re Conhaim*, 4 A. B. R. 58, 100 Fed. 268 (D. C. Wash.); *In re Harvey*, 10 A. B. R. 567, 122 Fed. 745 (D. C. Penn.); *In re Barr Pumping Engine Co.*, 11 A. B. R. 312 (Ref. Penn.); compare, *In re Force*, 4 A. B. R. 114 (Ref. Mass.); contra, *In re Veitch*, 4 A. B. R. 112, 101 Fed. 251 (D. C. Conn.).

Compare, contra, *In re Stalker*, 10 A. B. R. 709, 123 Fed. 961 (D. C. N.

Y.), where the doctrine seems to be laid down that where injustice will be done, the taxes will not be ordered paid out of the general estate. Also, that where sold subject to taxes, the purchaser will have to pay the taxes.

Compare, contra, *In re Broom*, 10 A. B. R. 427, 127 Fed. 639 (D. C. N. Y.). Compare dissenting opinion in *City of Waco v. Bryan*, 11 A. B. R. 481, 127 Fed. 59 (C. C. A. Tex.). Compare, contra, where property sold by trustee and taxes deducted from price, under law of 1867, *Foster v. Ingles*, 13 N. B. Reg. 239, Fed. Cas. 4973.

certificates are parties to this proceeding. Evidently they do not rely upon the redemption of the property by the trustee in bankruptcy, or the payment of the taxes as a preferred claim. The taxes were paid by them in full, and they hold the property taxed as security. What further interest has the county and city in the real estate in question? No other or different taxes are due and owing them from the estate of the bankrupt. The remedy which the county and city have elected for the collection of the tax has resulted in absolutely wiping out the unpaid liens for taxes, and in securing, if not absolutely paying, their claim. There is no sound reason why the county and city should longer be regarded as creditors entitled to a priority of payment."

But in the case *In re Brinker*, it will be observed, it was a purchaser, not the state or municipality itself, that was praying priority of payment.²⁹

It would seem that the true rule in cases of mortgaged property would be that the trustee should pay to the state, municipality or federal government as a priority claim, the taxes due it from the bankrupt out of the general fund, for he is ordered to do so by the express words of the statute, and as between the state and the bankrupt estate, the bankrupt estate is bound to pay the bankrupt's taxes as a priority claim, no matter if the state also has a lien therefor on the property itself; but, having done so, that the trustee then should be subrogated to the *lien* of the taxes thus paid by him, if there be any lien therefor, as between him and other parties. By such subrogation, the state would get its taxes without delay; the statute be obeyed; and yet the creditors not be prejudiced nor mortgagees unduly favored. The distinction must be constantly borne in mind between the tax as a priority claim and as a lien on property. As a priority claim it is absolutely to be paid first, regardless of liens or benefits; but it is to be paid solely to the state or municipality and is a priority claim only in so far as it is *owing* by the bankrupt himself *to the state or municipality*. As a lien, on the other hand, it takes its place (although the first place) among other liens; and the same rules and doctrines of subrogation, etc., apply as with other liens.

The court's reasoning in *In re Brinker*, 12 A. B. R. 122, 128 Fed. 634 (D. C. N. Y.), refusing to grant subrogation to the purchaser, does not militate against, but rather strengthens, the above position, for general creditors are forced to pay the taxes to save their assets and hence come within the rules as to subrogation.

Nor does the ruling in *In re Hollenfeltz*, 2 A. B. R. 499, 94 Fed. 629 (D. C. Iowa), refusing reimbursement out of rents collected by the trustee to a purchaser at foreclosure sale for taxes paid by him, that were a lien at the time of the purchase, militate against the rule, for in that case, it was not the state nor municipality that was claiming priority, but the purchaser was claiming subrogation.³⁰

29. To same effect as *In re Brinker*, see *In re Hollenfeltz*, 2 A. B. R. 499, 94 Fed. 629 (D. C. Iowa).

30. But *In re Force*, 4 A. B. R. 114 (Ref. Mass.), a remainderman furnish-

ing money for the paying of taxes properly payable by the bank life tenant, and doing so to save the estate, was held entitled to subrogation to the lien of the taxes thus paid off.

Nor can the trustee destroy the priority right of a tax-claimant by surrendering the property to a lienholder or abandoning it in a proceedings to which the tax-claimant is not a party.³¹

§ 2148. But Such Absolute Priority Belongs Solely to State, Municipality, etc., Not to One Who Has Paid or Holds Tax Title.—But the right to such priority of payment belongs solely to the state or municipality and does not inure to the benefit of one who has paid the taxes to the state or municipality and is now seeking reimbursement therefor, except, perhaps, where equity would declare the right of subrogation to exist.³²

In re Brinker, 12 A. B. R. 122, 128 Fed. 634 (D. C. N. Y.): "Such sales were made in conformity with statutory requirements providing for the collection of taxes. The city and county therefore have no real interest in the controversy. They are secure. * * *

"Such being the law, it is clear that third parties, bidders at a tax sale, holding tax certificates for their security, are not entitled to relief out of the assets of the bankrupt, much less is the purchaser at a foreclosure sale, having full knowledge of the tax liens, entitled to demand relief by the payment of taxes ostensibly to municipalities, but which in reality inure solely to his benefit, and when it may fairly be assumed that he bid in the incumbered property subject to existing liens for unpaid taxes and assessments."

In re Wyoming Valley Ice Co., 16 A. B. R. 597 (D. C. Pa.): "But to justify this, the tax in plain terms must be one which is due from the bankrupt, and not, as here, a mere liability for the collection of it from another."

"The treasurer of every corporation doing business in the State is thus bound to collect, in the manner prescribed, from resident bondholders, the tax which is so imposed, and, upon his failure to do so, the corporation is, no doubt, liable. But the cases, one and all, make it clear that the obligation of the corporation is one of collection only and does not make the tax its own."

Such person must rely on his lien if he have any. He is not entitled to priority of payment out of the general funds, except, perhaps, where equity would subrogate him thereto. And the mortgagee, himself bidding in the property, cannot require reimbursement for taxes paid by him that were a lien at the time he bid it in even out of the rent of the mortgaged property collected meanwhile by the trustee.³³ Similarly, a purchaser at a foreclosure sale in the state court, where the court has omitted to order taxes paid from the proceeds, will be refused subrogation, although he relied on the theory that the bankrupt estate must pay them.³⁴

Again, it has been held that a person paying taxes on real estate, bought by him of the bankrupt before bankruptcy under covenant against encum-

31. *Hecox v. County of Teller*, 28 A. B. R. 525, 198 Fed. 634 (C. C. A. Colo.).

32. *Cooper Grocery Co. v. Bryan*, 11 A. B. R. 734, 127 Fed. 815 (C. C. A. Tex.); compare, to same effect, *In re Broom*, 10 A. B. R. 427, 123 Fed. 639 (D. C. N. Y.); *In re Hibbler, etc., Co.*,

27 A. B. R. 612, 192 Fed. 741 (D. C. N. Y.).

33. *In re Hollenfeltz*, 2 A. B. R. 499, 94 Fed. 629 (D. C. Iowa).

34. *In re Brinker*, 12 A. B. R. 122, 128 Fed. 634 (D. C. N. Y.); *In re Hibbler*, 27 A. B. R. 612, 192 Fed. 741 (D. C. N. Y.).

branches, is not subrogated to the right of the state to priority of payment of taxes that the bankrupt thus should have paid.³⁵ Likewise, where the taxes are assessed against the lessor of the bankrupt but the bankrupt is under covenant to pay the same, the tax is not entitled to priority out of the bankrupt estate—the debt of the estate is to the landlord upon the covenant, not to the municipality or state upon the tax.³⁶

And a sale “subject to encumbrances” includes a lien for taxes; and the purchaser has no standing to apply for an order to pay the taxes out of the general estate.³⁷ Much less would such a purchaser have standing to apply for reimbursement, where he has already paid the taxes, even though the court might have ordered payment of taxes out of the proceeds of sale but did not do so.³⁸

But, where a sale of a stock of goods by the trustee in bulk is made “free and clear,” there being no provision in the order for payment of taxes from the proceeds, the state law fixing a lien therefor on the goods sold, the purchaser is entitled to have the tax lien paid out of the proceeds.³⁹ Of course, such payment would be by way of payment of the tax lien, not by way of payment of the tax as a priority claim.

It is constantly to be borne in mind that a tax may be not only a “priority” claim; but, if a lien, also a “secured” claim, and that the present propositions are concerned with it simply as a “priority” claim.

§ 2149. But “Subrogation” to Tax Lien Sometimes Proper.—But a remainderman or other party in interest, paying or furnishing money for the paying of taxes that ought to have been paid by the bankrupt in order to save the estate, may be entitled to subrogation to the amount of the tax lien so paid.

In *re Force*, 4 A. B. R. 114 (Ref. Mass.): “When the trustee was appointed, the taxes for 1898 were due and unpaid, and I think it was his duty to pay them out of the first money that came into his hands to a sufficient amount, and as the taxes for 1899 became a lien upon the property during his trusteeship, I think it would have been his duty to pay those also, if he had the requisite funds. *Re Tilden*, 1 Am. B. R. 300; *Re Baker*, 1 Am. B. R. 526. Nothing was paid by him, however, on account of these taxes, but they have been paid as above stated, and the amount deducted from what the petitioning heirs would have received from the proceeds of the sale of the property above the amount of

35. *Cooper Grocery Co. v. Bryan*, 11 A. B. R. 734, 127 Fed. 815 (C. C. A. Tex.).

36. In *re Broom*, 10 A. B. R. 427, 123 Fed. 639 (D. C. N. Y.).

37. In *re Hollenfeltz*, 2 A. B. R. 499, 94 Fed. 629 (D. C. Iowa); In *re Stalker*, 10 A. B. R. 709, 123 Fed. 961 (D. C. N. Y.).

38. In *re Gerry*, 7 A. B. R. 459, 112 Fed. 958 (D. C. Penn.); In *re Hollenfeltz*, 2 A. B. R. 499, 94 Fed. 629 (D. C. Iowa).

Sale of several parcels for lump sum,

the owner of the lien for taxes upon some of the parcels having notice and not objecting thereto, and the sale being “subject to encumbrances,” such lienholder is not entitled to payment out of the proceeds, it being impossible to identify the fund derived from the sale of his two parcels from the rest. In *re Gerry*, 7 A. B. R. 461, 112 Fed. 958 (D. C. Penn.).

39. In *re Keller*, 6 A. B. R. 351, 109 Fed. 131 (D. C. Iowa). Compare, to same effect, In *re Hilberg*, 6 A. B. R. 714 (Ref. Pa.).

the incumbrance upon it. This, I think, may be taken to be so far a payment on their part of these taxes as to give them an equitable claim upon the funds in the trustee's hands, according to the doctrine of subrogation, which is, as stated in *Sheldon on the Law of Subrogation*, § 11, that 'one who has been compelled to pay a debt which ought to have been paid by another, is entitled to indemnity from the funds out of which should have been made the payment which he has made.' It is true that these petitioners did not actually pay the money, but they are left in the same position financially as if they had. The life tenant should have paid these taxes out of the rents, and this duty devolved upon the trustee, if not as a burden attached to the life estate, yet it nevertheless became such under the specific terms of the Bankrupt Act, and if they were not paid, the property could and would have been sold by the city at the expense of the remaindermen. Such a sale was not, in fact, made, but in accounting for the proceeds of the foreclosure sale, the mortgagee deducted the amount of the taxes, thus giving these petitioners, as I believe, an equitable standing."

Or a mortgagee, judgment creditor or even general creditor, may likewise be entitled to subrogation if he makes the payment to save the estate, or otherwise makes it under circumstances entitling him to subrogation in equity.

Obiter, inferentially, In *re Brinker*, 12 A. B. R. 122, 128 Fed. 634 (D. C. N. Y.): "Nor does the principle of the right of equitable subrogation have application here. *Acer v. Hotchkiss*, 97 N. Y. 396. The purchasers of the tax certificates were not obliged to bid in the property at the tax sale in order to protect themselves. They were not mortgagees or judgment creditors, or even creditors, of the bankrupt. They are third parties to the transaction, pure and simple, and accordingly cannot invoke the aid of the doctrine of subrogation. Furthermore, none of the purchasers of the tax certificates are parties to this proceeding. Evidently they do not rely upon the redemption of the property by the trustee in bankruptcy, or the payment of the taxes as a preferred claim. The taxes were paid by them in full, and they hold the property taxed as security."

But such right of subrogation would not exist, of course, in favor of a mere purchaser, though he bought in reliance upon the estate being obliged to pay the taxes.⁴⁰

In *re Hibbler*, 27 A. B. R. 612, 192 Fed. 741 (D. C. N. Y.): "While ordinarily the taxes legally due and owing by the bankrupt must be paid by his trustee before the assets of the bankrupt are apportioned among the creditors, still, when the property is sold under an order of the court, and the purchaser subsequently pays the taxes, he is not subrogated to the rights of the municipality to priority payment.

"By analogy it may safely be held, I think, that when the trustee in bankruptcy transfers property subject to the payment of taxes, there is a legal obligation on the part of the grantee to make such payment; and, if the property is by him sold, the purchaser, having knowledge of outstanding taxes cannot be subrogated to the rights of the municipality for preferential payment."

§ 2150. Must Be Owing by Bankrupt and Assessed against Him.
—The tax must be owing by the bankrupt and be owing by him to the mu-

40. In *re Brinker*, 12 A. B. R. 122, 128 Fed. 634 (D. C. N. Y.).

nicipal, state or federal government,⁴¹ and a mere obligation on the bankrupt's part, as tenant for instance, to pay the tax levied upon the property in the landlord's name, does not entitle the tax to priority of payment out of the tenant's estate, the debt of the estate being upon the covenant, not upon the tax.

In *re Broom*, 10 A. B. R. 428, 123 Fed. 639 (D. C. N. Y.): "The only liability of the bankrupt for the taxes specified, and which is sought to be allowed as a preferred claim, is a contractual one between the bankrupt and the Flour City National Bank, and therefore cannot be regarded as a tax owing from the bankrupt to any municipality, within the provisions of § 64 (a).

But while such tax may not be entitled to priority of payment as a "priority" claim under § 64 (a), yet, if it be also a *lien* on the property, its security will, of course, remain unimpaired.

Nor does a mere obligation on a bankrupt corporation to collect taxes from bondholders entitle them to priority out of the bankrupt's estate.⁴²

Obiter, In *re Wyoming Valley Ice Co.*, 21 A. B. R. 1, 165 Fed. 789 (D. C. Pa.): "But * * * as to the taxes on corporate loans, it was held [in *re Wyoming Valley Ice Co.*, 16 A. B. R. 594, 145 Fed. 267] that being due in realty from bondholders, the company [bankrupt] being merely a collector, they are not a tax as to it, but merely a liability arising out of the duty to collect imposed by the statute, and were not therefore entitled to the priority of payment contended for."

And where the corporation has failed to collect such a tax or to pay it over to the state, a claim by the state will be allowable only as a general claim.

Pennsylvania v. York Silk Mfg. Co., 27 A. B. R. 525, 192 Fed. 81 (C. C. A. Pa.): "It appears also, that the bankrupt on September 1, 1908, issued its bonds for the sum of \$750,000, and secured them by a mortgage upon its real estate. By a statute of the State of Pennsylvania it is made the duty of the treasurer of a corporation, if the holder be a resident of Pennsylvania, to deduct from the interest the tax imposed by the State upon such bond and pay the same into the State treasury. This is a tax against the holder of the bond, and not against the corporation. The corporation, acting through its treasurer, is charged with the duty of collecting the tax and paying it over to the State. If it fails so to do, it becomes liable to the State for the amount of the tax and the penalty prescribed. Such is the purport of the decisions. In *re Wyoming Valley Ice Co.* (D. C. Pa.), 16 A. B. R. 594, 145 Fed. 267; *Commonwealth v. Railroad Co.*, 186 Pa. 247, 40 Atl. 1132. But there is nothing in the law giving to the State a preferred claim against the corporation whose treasurer has failed to collect the tax or to pay it over to the State. Consequently the item of \$2,640 in the claim now under consideration for 'tax on corporate loans in the amount of \$750,000 for 1909, and 10 per cent. penalty,' is not allowable as a preferred claim, but as the court below held, is allowable as a general one. There is one other item in the claim. It is for \$500 for 'penalty

⁴¹ In *re Wyoming Valley Ice Co.*, 16 A. B. R. 594, 145 Fed. 267 (D. C. Pa.).

⁴² *Pennsylvania v. York Silk Mfg.*

Co., 27 A. B. R. 525, 192 Fed. 81 (C. C. A. Pa.), affirming *In re York Silk Mfg. Co.*, 26 A. B. R. 650, 188 Fed. 735).

for failure to file capital stock reports, 1903 to 1909, inclusive.' This item, like the one for \$5,000 above mentioned, the court below disallowed without prejudice to the filing of a new claim under § 57j. This is all the commonwealth can properly ask for."

§ 2151. Firm Taxes in Individual Bankruptcies.—Where the state law makes a partner individually liable for taxes assessed against the firm, they must be paid from his individual estate in bankruptcy as a priority claim.⁴³

An individual partner's personal tax is not to be paid out of firm assets, in a partnership bankruptcy, until firm creditors are paid.⁴⁴

§ 2152. Funds in Hands of Trustee Taxable, Where Taxable if Similarly Sequestered by State Legal Proceedings.—Funds in the hands of the trustee are taxable which would be taxable in that particular taxing district, if similarly sequestered by other legal custody.⁴⁵

Swarts v. Hammer, 9 A. B. R. 691, 120 Fed. 256 (C. C. A. Mo.): "The money was clearly liable to be taxed under the State law and the tax is valid and collectible, unless the Bankrupt Act exempts it from taxation. Exemption from taxation is never presumed. The legislative intent to exempt property from taxation must be clearly and explicitly expressed. Whether Congress could rightfully exempt from State taxation the property of a bankrupt in the hands of a trustee in bankruptcy, and otherwise subject to taxation, we need not inquire. It has not attempted to do so, and it is highly probable it never will. The power of taxation, as well as the power to exempt from taxation, is a legislative, and not a judicial, function; and a bankrupt court, no more than any other court, can exempt from taxation property in the hands of one of its officers which is liable to taxation under the State Law. It has never been questioned, but what property in the custody and control of receivers and trustees of the Federal courts was subject to taxation under the State law, the same as other like property. Judson on Taxation, § 407, and cases cited. And this applies to trustees in bankruptcy as well as receivers and trustees in other cases and proceedings in the Federal courts. It is a grave mistake to suppose that property in the possession and custody of an officer of the Federal court by that single fact enjoys immunity from taxation."

Swarts v. Hammer, 11 A. B. R. 708, 194 U. S. 441, affirming 9 A. B. R. 691: "By the transfer to the trustee, no mysterious or peculiar ownership or qualities are given to the property. It is dedicated, it is true, to the payment of the creditors of the bankrupt, but there is nothing in that to withdraw it from the necessity of protection by the State and municipality or which should exempt it from its obligations to either."

In re Prince & Walter, 12 A. B. R. 679, 131 Fed. 546 (D. C. Pa.): "But the Bankruptcy Act does not withdraw the estates of bankrupts from the reach of the taxing power, and they are subject in consequence, to the payment of taxes imposed while they are in the hands of trustees, the same as if they were not. * * * Even though accruing after bankruptcy, they must be re-

43. *In re Green*, 8 A. B. R. 553, 116 Fed. 118 (D. C. Iowa).

44. *In re Flatau & Stern*, 21 A. B. R. 352 (Ref. N. Y.).

45. *In re Fisher & Co.*, 17 A. B. R.

412 (D. C. N. J.); inferentially, to that effect, *In re Keller*, 6 A. B. R. 351, 109 Fed. 131 (D. C. Iowa); *City of Waco v. Bryan*, 11 A. B. R. 481, 127 Fed. 79 (C. C. A. Tex.).

garded as within the meaning of the statute, and entitled to priority, the same as those which antedate it."

In *re Sims*, 9 A. B. R. 162, 118 Fed. 356 (D. C. Pa.), where the court says: "It does not follow, of course, that all moneys deposited in the registry of the court or designated depository of the courts are subject to taxation. Much of it belongs to nonresidents, and would not be subject to state taxes merely because impounded in litigation. But when a fund is held by a trustee in bankruptcy or other fiduciary agent of the court, which, but for the litigation, would have been liable for taxation in a particular taxing district, we see no reason why the court should not, on proper application, direct the payment of current assessments of valid taxes."

In *re Conhaim*, 4 A. B. R. 59, 100 Fed. 268 (D. C. Wash.): "The manifest intent of the law is that, while the estate is in the hands of the trustee, his custody shall not constitute a barrier to prevent the collection of taxes which would be collectible under the law if the property had remained in the possession and control of the bankrupt himself."

§ 2152½. Broad Use of Term "Tax" in Bankruptcy.—It is obvious that the word "tax" as used in the Bankruptcy Act is not used in any restricted or narrow sense.

In *re Lange Co.*, 20 A. B. R. 478, 159 Fed. 586 (D. C. Iowa): "It is obvious that the word 'tax,' as used in the Bankruptcy Act, is not used in any restricted or narrow sense, but is used broadly to include all obligations imposed by the State and general governments under their respective taxing or police powers for governmental or public purposes. That a tax so imposed may not be a general property tax does not deprive it of the character of a tax. Many taxes are imposed under the name of license fees, franchise taxes, or taxes for special purposes under some other name, and are therefore special taxes; but they are nevertheless taxes imposed for a public purpose, no matter what the name under which they are levied or imposed, and are clearly within the meaning of the term 'tax' as used in the Bankruptcy Act."

It includes personal taxes.⁴⁶

§ 2153. "Tax" Includes Assessment for Local Improvements.—"Tax" as meant in the Bankruptcy Act includes an assessment for local improvements.⁴⁷

§ 2154. Nature of Tax, Whether License, Penalty or Tax, Generally Determined by State Law.—The nature of a "tax," whether a mere license, or actually a tax, is, in general, to be determined by the law of the state imposing it.⁴⁸

In *re Ott*, 2 A. B. R. 637, 95 Fed. 274 (D. C. Iowa): "We now turn to the consideration of the construction of this statute by the Supreme Court, the highest judicial tribunal of the State. Such construction, if directly and positively given, and upon the sections above cited with respect to the question herein involved ['mulct tax'] is at least to be given careful and weighty consideration,

^{46.} In *re Flatau & Stern*, 21 A. B. R. 352 (Ref. N. Y.).

^{47.} In *re Stalker*, 10 A. B. R. 709, 123 Fed. 961 (D. C. N. Y.).

^{48.} *First Nat'l Bk. v. Aultman, Miller & Co.*, 12 A. B. R. 12 (Ref. Ohio): A case of franchise tax.

and may control the decision reached herein. Indeed, the opposing creditors contend it must control such decision."

In *re Stalker*, 10 A. B. R. 709, 123 Fed. 96 (D. C. N. Y.): "This question is broad [whether 'assessment' a 'tax'] and might be of much difficulty, were it not that the interpretation adopted by the highest tribunal of the State, must govern here. It is an established rule in the courts of the United States that the decisions of the State courts with regard to the law of real estate, construction of State constitutions and statutes, are authoritative rules of what the law is."

Thus, water rates have been held to be "taxes" in Pennsylvania⁴⁹ and in New York,⁵⁰ but in New York to be taxes against the landlord and not entitled to priority of payment out of the bankrupt tenant's estate.⁵¹ And the "Mullet tax" of Iowa has been held not to be a "tax" entitled to priority of payment, but a mere license fee to conduct a saloon,⁵² although this holding is perhaps incorrect even in accordance with Iowa law;⁵³ while the "cigarette tax" of the same state has been held to be a "tax."⁵⁴

A statutory duty imposed on corporations to collect a tax from the holders of its obligations, is not itself a tax.⁵⁵

§ 2155. But Not Always.—But if the legislature of a state gives the name of "tax" to an exaction which is not a tax, and the courts of the state join in the misnomer, the bankruptcy courts, nevertheless, are not required to disregard the substance of the thing to the detriment of other claimants.⁵⁶

State of N. J. v. Anderson, 203 U. S. 483, 17 A. B. R. 68: "It is doubtless true, as was said in the opinion of the learned judge speaking for the Circuit Court of Appeals, in this case, that if the highest court of the State should decide that a given statute imposed no tax within the meaning of the law as interpreted by it, a Federal court, in passing upon the Bankruptcy Act, would not compel the State to accept a preference from the bankrupt's estate upon a different view of the law. Conceding the doctrine that the meaning of a statute is a State question, except where rights, the subject of adjudication by the Federal courts, have accrued before its construction by the State court, or the question of contract within the protection of the Federal Constitution is involved, still a State court, while entitled to great consideration, cannot conclusively decide that to be a tax within the meaning of a Federal law, providing for the payment of taxes, which is not so in fact."

^{49.} In *re Industrial Cold Storage & Ice Co.*, 20 A. B. R. 904, 163 Fed. 390 (D. C. Pa.).

^{50.} In *re Broom*, 10 A. B. R. 427, 123 Fed. 639 (D. C. N. Y.).

^{51.} In *re Broom*, 10 A. B. R. 427, 123 Fed. 639 (D. C. N. Y.).

^{52.} In *re Ott*, 2 A. B. R. 637, 95 Fed. 274 (D. C. Iowa), evidently reversed by later decisions. See, In *re Lange Co.*, 20 A. B. R. 478, 159 Fed. 586 (D. C. Iowa).

^{53.} In *re Lange Co.*, 20 A. B. R. 478, 159 Fed. 586 (D. C. Iowa).

^{54.} In *re Lange Co.*, 20 A. B. R. 478, 159 Fed. 586 (D. C. Iowa).

^{55.} In *re York Silk Mfg. Co.*, 26 A. B. R. 650, 188 Fed. 735 (D. C. Pa., affirmed sub nom. *Pennsylvania v. York Silk M'fg Co.*, 27 A. B. R. 525, 192 Fed. 81); *Pennsylvania v. York Silk M'fg Co.*, 27 A. B. R. 525, 192 Fed. 81 (C. C. A. Pa., affirming In *re York Silk M'fg Co.*, supra).

^{56.} In *re Cosmopolitan Power Co.*, 14 A. B. R. 604, 137 Fed. 858 (C. C. A. Ills., affirming 13 A. B. R. 39, but itself reversed, on other grounds, in *State of N. J. v. Anderson*, 17 A. B. R. 68, 203 U. S. 483); In *re Lange Co.*, 20 A. B. R. 478, 159 Fed. 586 (D. C. Iowa).

A bonus required by the state on an increase of the capital stock of a corporation is not a tax, and, therefore, is not entitled to priority; but it may be allowed as a general claim.⁵⁷

So, a penalty due, under the local law, for the failure of a corporation to deduct a tax from the interest due its bondholders, and pay to the state, is not a tax imposed on the bonds.⁵⁸

§ 2156. Thus, Franchise Tax.—Thus, it has finally been settled by the Supreme Court of the United States, although with a strong dissenting opinion, that the so-called “franchise tax” of New Jersey, a type of many similar impositions, is a “tax” within the meaning of § 64 (a).⁵⁹

State of New Jersey v. Anderson, 203 U. S. 483, 17 A. B. R. 68 (reversing *In re Cosmopolitan Co.*, 14 A. B. R. 604, 137 Fed. 858, C. C. A. Ills.): “We are of opinion that this claim was for a tax. The language of the Act, as we have said, is very broad and includes all taxes. It is not necessary to enter upon a discussion of the different forms which taxes may take. Generally speaking, a tax is a pecuniary burden laid upon individuals or property for the purpose of supporting the government. We think this exaction is of that character. It is required to be paid by the corporation after organization, in invitum. The amount is fixed by the statute, to be paid on the outstanding capital stock of the corporation each year, and capable of being enforced by action against the will of the taxpayer. * * *

“It is urged by the appellee, and upon this ground the case was decided in the Circuit Court of Appeals, that this is in no just sense a tax levied by the State, but is the result of a contract by which the corporation was brought into existence, the consideration being the payment of annual sums for the privileges given by the State, for which no lien is given upon the property, but only a right of action for their recovery. But this imposition is in no just sense a contract. The amount to be paid, fixed by the statute, is subject to control and change at the will of the State. It is imposed upon all corporations, whether organized before or after the passage of the Act. The corporation is not consulted in fixing the amount of the tax, and under the laws of New Jersey the charter of such corporations as this may be amended or repealed.”

Although the strong dissenting opinion expressed by Justice Harlan is to be noted:

“The Chief Justice, Mr. Justice Peckham and myself dissent from the opinion of the court. In our judgment the ‘taxes’ owing by a bankrupt to a State—which § 64a of the Bankruptcy Act provides shall be paid in advance of the payment of dividends to creditors—do not embrace an ‘annual license fee or franchise tax’ (the words of the New Jersey statute), which, strictly, is not a property tax, but only an exaction by the State for the privilege given to a cor-

⁵⁷. *Pennsylvania v. York Silk Mfg. Co.*, 27 A. B. R. 525, 192 Fed. 81 (C. C. A. Pa., affirming *In re York Silk Mfg. Co.*, 26 A. B. R. 650, 188 Fed. 735).

⁵⁸. *Pennsylvania v. York Silk Mfg. Co.*, 27 A. B. R. 525, 192 Fed. 81 (C. C. A. Pa., affirming *In re York Silk Mfg. Co.*, 26 A. B. R. 650, 188 Fed. 735).

⁵⁹. *In re Mutual Mercantile Agency*, 8 A. B. R. 435 (Ref. N. Y.); *In re Halsey Electric Generator Co.*, 23 A. B. R. 401, 175 Fed. 825 (D. C. N. J.); contra, *In re Danville Rolling Mill Co.*, 10 A. B. R. 327, 121 Fed. 432 (D. C. Pa.).

Adjudication of a Corporation as a Bankrupt, Not a “Dissolution” of It.—See ante, § 451½.

poration to do certain business under its charter. We think the Bankruptcy Act should be so construed. It cannot be otherwise construed without doing gross injustice to those creditors of the bankrupt corporation who have business transactions with it at its place of business. Here the bankrupt corporation did no business in New Jersey. So far as appears, it did not have, nor expect to have, any connection with that State except to become incorporated under its laws. It had its seat of operations and all its tangible property in the State of Illinois. It had no property in New Jersey. Its scheme was to get a charter from New Jersey and then go to another State for purposes of its business. We do not think that Congress intended that in the distribution of the assets of a bankrupt preference should be given to the claims of a State which have their origin in and are wholly based upon a bargain with the State whereby certain privileges are granted in exchange for certain payments—privileges which the State may grant or withhold at pleasure. In our opinion the word 'taxes' in the Bankruptcy Act was intended to embrace only burdens or charges imposed in invitum and which were in their nature and in reality 'taxes,' as distinguished from governmental exactions for privileges granted. The claim of New Jersey, whatever its true amounts, should not be given priority, but should be placed upon the same footing with claims of other creditors. This view is consistent with the Act of Congress."

And it has been held entitled to priority as a tax, even though it is not assessed until after the adjudication, if for a period anterior thereto.⁶⁰

A sum exacted by the state for the privilege of increasing corporate stock is not a tax.⁶¹

§ 2157. But Bankruptcy Court, Forum as to Amount and Legality of Tax.—But the Bankruptcy Court is the forum for the determination of the validity of the tax and all questions in relation thereto.⁶²

§ 2158. And Decision of State Board of Assessment Not "Res Judicata."—The determination, after due hearing, before bankruptcy, by the State Board of Assessment or other state tribunal having in charge the settlement of disputes over the amount of taxes, is not *res adjudicata* in bankruptcy.⁶³

§ 2159. Nor Is Failure to Pursue Statutory Appeal or Abatement Fatal.—Nor is the previous failure of the bankrupt to follow the pre-

60. *State of N. Jersey v. Anderson*, 17 A. B. R. 68, 203 U. S. 483; *contra*, *First Nat'l Bk. v. Aultman-Miller & Co.*, 12 A. B. R. 12 (Ref. Ohio).

61. *In re York Silk Mfg. Co.*, 26 A. B. R. 650, 188 Fed. 735 (D. C. Pa., affirmed sub nom. *Pennsylvania v. York Silk Mfg. Co.*, 27 A. B. R. 525, 192 Fed. 81 (C. C. A.); *Pennsylvania v. York Silk Mfg. Co.*, 27 A. B. R. 525, 192 Fed. 81 (C. C. A. Pa., affirming *In re York Silk Mfg. Co.*, 26 A. B. R. 650, 188 Fed. 735).

62. Bankr. Act, § 64 (a): "And in case any question arises as to the amount or legality of any such tax, the same shall be heard and determined by the court."

State of New Jersey v. Anderson, 17 A. B. R. 68, 203 U. S. 483; *In re Cosmopolitan Power Co.*, 14 A. B. R. 604, 137 Fed. 858 (C. C. A. Ills., affirming 13 A. B. R. 39); *In re Selwyn Importing Co.*, 18 A. B. R. 191 (Ref. N. Y.); *In re [Otto Freund] Arnold Yeast Co.*, 24 A. B. R. 458, 178 Fed. 305 (D. C. N. Y.).

63. *State of N. Jersey v. Anderson*, 17 A. B. R. 68, 203 U. S. 483; *In re Cosmopolitan Power Co.*, 14 A. B. R. 604, 137 Fed. 858 (C. C. A. Ills., affirming 13 A. B. R. 39). Compare, *In re Wyoming Valley Ice Co.*, 21 A. B. R. 1, 165 Fed. 789 (D. C. Pa.).

scribed statutory method for obtaining review or abatement of the tax, fatal to the re-examination in bankruptcy.⁶⁴

And a tax which, because of failure to take action for review within the statutory time, could not be reviewed in the state courts, may nevertheless be reviewed in the bankruptcy court, under the special provisions of Bankruptcy Act, § 64 (a).⁶⁵

§ 2160. Whether Taxes "Provable" Debts.—Taxes are not debts in the ordinary sense of that word. They are demands levied for the support of government or for some special purpose authorized by it.⁶⁶ There is considerable strength in the contention, however, that they are provable "debts" or "demands" within the meaning of the bankruptcy term, although the form of proof thereof and the limitations as to time, etc., be not the same as in cases of other debts. To be sure, § 63, defining "provable" debts, does not mention taxes, and they are thus not within the letter of §§ 1 (9) and (11), defining "debt" as being "any debt, claim or demand provable" in bankruptcy and "creditor" as being the "owner" of such provable debt. yet § 17, in enumerating the obligations excepted from the operation of a discharge in bankruptcy, says "all *provable* debts except (1) *taxes*, etc.," thus furnishing the implication that taxes are provable debts.⁶⁷

Obiter, In re United Button Co., 15 A. B. R. 400, 140 Fed. 495 (D. C. Del.): "A tax is not strictly a debt. It lacks the nature of a debt in that, though for a sum certain, it is not founded upon any agreement or assent of the person or persons against whom it is assessed, but is a burden for public purposes imposed in invitum. As an obligation or duty created by statute to pay money, however, it is quasi contractual, although there may be difficulty as to the remedy for its enforcement in a given case. Keener, in his work on Quasi-Contracts, p. 16, states that 'a statutory obligation which does not rest upon the consent of the parties, is clearly quasi contractual in its nature.' This proposition is illustrated by the case of a statutory demand for half pilotage for refusal to accept the services of a pilot. Steamship Co. v. Joliffe, 2 Wall. 450, 457. There has been

⁶⁴. In re Selwyn Importing Co., 18 A. B. R. 191 (Ref. N. Y.); In re [Otto Freund] Arnold Yeast Co., 24 A. B. R. 458, 178 Fed. 305 (D. C. N. Y.).

⁶⁵. In re [Otto Freund] Arnold Yeast Co., 24 A. B. R. 458, 178 Fed. 305 (D. C. N. Y.).

⁶⁶. Hecox v. County of Teller, 28 A. B. R. 525, 198 Fed. 634 (C. C. A. Colo.); obiter, In re United Button Co., 15 A. B. R. 400, 140 Fed. 495 (D. C. Del.); Meriwether v. Garrett, 102 U. S. 472; In re Fisher & Co., 17 A. B. R. 411, 148 Fed. 907 (D. C. N. J.); In re Kallak, 17 A. B. R. 415, 147 Fed. 276 (D. C. N. Dak.).

⁶⁷. In re Cleanfast Hosiery Co., 4 A. B. R. 702 (Ref. N. Y.); compare, query, In re Beddingfield, 2 A. B. R. 355; compare, In re Prince & Walter, 12 A. B. R. 679 (D. C. Pa.), quoted at § 2161; In re Flatau & Stern, 21 A.

B. R. 352 (Ref. N. Y.); obiter, In re Schuyler & Co., 21 A. B. R. 428 (Ref. N. Y.).

Compare, in other connection, however, Meriwether v. Garrett, 102 U. S. 472: "Taxes are not debts. It was so held by this court in the case of Oregon v. Lane County, reported in 7 Wallace. Debts are obligations for the payment of money founded upon contract, express or implied. Taxes are imposts levied for the support of the government, or for some special purpose authorized by it. The consent of the tax payer is not necessary to their enforcement. They operate in invitum. Nor is their nature affected by the fact that in some States—and we believe in Tennessee—an action of debt may be instituted for their recovery. The form of procedure cannot change their character."

much conflict in the decisions with respect to procedure for the collection of taxes, where no statutory mode has been prescribed, and also upon the point whether and under what circumstances, notwithstanding the existence of a statutory mode, the general principles of law will furnish an alternative or cumulative remedy by action. These matters of dispute, however interesting in themselves, are unimportant here. The procedure is supplied by the Bankruptcy Act. Section 64, which deals, among other things, with the priority of debts and demands against the estate of a bankrupt, provides, in paragraph a, for the payment by the trustee under the order of the court of 'all taxes legally due and owing by the bankrupt to the United States, state, county, district or municipality, in advance of the payment of dividends to creditors,' and that 'in case any question arises as to the amount or legality of any such tax the same shall be heard and determined by the court.' Thus, the taxes enumerated in § 17, 'legally due and owing by the bankrupt,' by § 64 are directed to be paid out of the estate, by § 17 are recognized as 'provable debts,' and are demands of a quasi contractual nature. While strict or technical 'proof' of them is not required, although often presented, there can be no doubt that they are to be treated as provable debts or demands embraced in the class 'founded upon an open account, or upon a contract express or implied.'"

In *re Fisher & Co.*, 17 A. B. R. 411, 148 Fed. 907 (D. C. N. J.): "While taxes are not in a strict sense, debts, they are so denominated in the Bankruptcy Act. Section 17 * * * Section 64 * * * and § 1 declare that the word "debt" shall include any debt, demand or claim provable in bankruptcy. Of course a tax is provable in bankruptcy."

Contra, In *re Kallak*, 17 A. B. R. 415, 147 Fed. 276 (D. C. N. Dak.): "* * * public taxes do not constitute a 'claim' in bankruptcy."

§ 2161. No Formal "Proof" Required: Trustee Must Search for Taxes.—Taxes need not be sworn to and no formal proof of claim is required. It is the trustee's duty to search for taxes and his only necessary voucher is the ordinary receipt for taxes.⁶⁸

In *re Prince & Walter*, 12 A. B. R. 679, 131 Fed. 546 (D. C. Penn.): "And the Bankruptcy Act evidently does not contemplate that they shall be proved like an ordinary debt; providing, as it does, that they shall be paid by the trustee on the order of the court, and that he shall have credit in his accounts upon filing the receipts of the proper officers therefor."

In *re Harvey*, 10 A. B. R. 567, 122 Fed. 745 (D. C. Pa.): "An adjudication in bankruptcy does not affect such a lien, nor impose upon the city the duty of proving its claim as an ordinary creditor must do."

In *re Fisher & Co.*, 17 A. B. R. 412, 148 Fed. 907 (D. C. N. J.): "* * * and the injunction of § 64 (a) is that the court 'shall order' the trustee to pay them. It seems to be the duty of the court to require such payment, even though no claim for the same shall have been presented in the manner or within the time prescribed by the Bankruptcy Act for the filing of claims."

In *re Cleanfast Hosiery Co.*, 4 A. B. R. 702 (Ref. N. Y.): "Section 64 of the Act relates specifically to taxes, and provides a special method for their payment, to wit, that the court shall order the trustee to pay them, and that the

68. Bankr. Act, § 64 (a): "Upon filing the receipts of the proper public officers for such payment he shall be credited with the amount thereof, and in case any question arises as to the amount or legality of any such tax the

same shall be heard and determined by the court." In *re Kallak*, 17 A. B. R. 415, 147 Fed. 276 (D. C. N. Dak.); inferentially, In *re Monsarrat* (No. 2), 25 A. B. R. 820 (D. C. Hawaii). Compare, post, § 2192.

receipt of the proper officer shall entitle the trustee to a credit for the amount paid. A formal proof of claim, as in case of provable debts generally, is not specifically required; in fact, the latter provision as to a receipt by the proper officer would seem to imply that none is necessary, and no time limit is imposed. I think this section should in these respects control, rather than § 57, subdivision 'n,' above mentioned, prescribing the rule as to provable debts as a class, under the familiar rule of construction, that a statutory provision as to a general class must give way to a special provision relating to one of the class."

§ 2162. Year's Limitation for "Proof" Not Applicable to Taxes.

—The limitation of one year for the proof of claims does not apply to taxes.⁶⁹

§ 2163. Tax Not Such "Secured" Claim as Requires Exhaustion of Security.—Taxes do not constitute a "secured" claim within the intent of the provisions of § 57, requiring deduction of the value of the security held and allowance only for the deficit.⁷⁰ Rather, they are secured claims, to be sure, if a lien on the property by law, but they are also "priority" claims, and, being priority claims, are entitled to priority of payment regardless of the security.

DIVISION 2.

WORKMEN, CLERKS, SALESMEN AND SERVANTS.

§ 2164. "Wages of Workmen, Clerks, Salesmen and Servants."

—After taxes, the next in order of priority of distribution are the wages due to workmen, clerks, travelling or city salesmen or servants, which have been earned within three months before the date of the commencement of the proceedings, not to exceed three hundred dollars.⁷¹

§ 2165. Must Be "Wages," and Be "Due" and "Earned."—It is for "wages" that the priority is given,⁷² and for such wages as are "due" and "earned."⁷³ But "wages" may include payments for piece work or by commissions⁷⁴ in the employ of the bankrupt.⁷⁵

§ 2166. Thus, No Priority for Damages for Breach of Contract of Employment.—It is for wages earned that the priority is given and

69. In re Cleanfast Hosiery Co., 4 A. B. R. 702 (Ref. N. Y.); In re Fisher & Co., 17 A. B. R. 411, 148 Fed. 907 (D. C. N. J.). Compare, post, § 2193.

70. In re Harvey, 10 A. B. R. 567, 122 Fed. 745 (D. C. Pa.).

71. Bankr. Act, § 64 (b) (4). In re Rose, 1 A. B. R. 69 (Ref. Ohio); In re Blackstaff Engineering Co., 29 A. B. R. 663, 200 Fed. 1019 (D. C. Ga.); In re Van Wert Machine Co., 26 A. B. R. 597, 186 Fed. 607 (D. C. Mass.); Guarantee, etc., Co. v. Title, etc., Co., 224 U. S. 152, 27 A. B. R. 873.

In re Strickland, 20 A. B. R. 923 (Ref. Ga.), although in this case the

referee erroneously allowed the wages to have priority over exemptions!

Law in Force at Date of Adjudication Controls.—The right of priority will be determined in each case by the law as it stood at the date of the adjudication. In re Photo Engraving Co., 19 A. B. R. 94, 155 Fed. 684 (D. C. N. Y.).

72. "Wages."—See In re Fink, 20 A. B. R. 897, 163 Fed. 135 (D. C. Pa.).

73. Bankr. Act, § 64 (b) (4).

74. See §§ 2170½, 2175.

75. In re Dunn, 25 A. B. R. 103, 181 Fed. 701 (D. C. N. Y.).

damages for breach of contract of employment are not entitled as such to priority.⁷⁶

In *re Lewis Co.*, 12 A. B. R. 279 (Ref. R. I.): "When a salesman employed under a yearly contract is wrongly discharged after seven weeks of work, sues at once and recovers judgment for breach of such contract, the amount recovered is not wages; hence upon the bankruptcy of the employer within a year, the salesman is not entitled to payment in full for the proportionate part of his judgment, which three months bears to the unexpired period of his term of service. * * *

"In the first place, it seems to the referee that the present claim is not for wages as defined above. It is a sum fixed upon by the court as the amount to be paid by E. B. Lewis Company because it wrongfully refused to allow Crooker to earn wages. The net results may be the same, but the referee is unwilling to read into the law, 'Damages for breach of wage contract,' as seems necessary in order to support claimant's contention. By way of illustration, would it be contended that this claim was for wages if claimant had secured a place elsewhere at a salary of \$10 per week and claimed the other \$10 for loss of wages as a measure of damages against the E. B. Lewis Co.? Does not this show that the real nature of the claimant's demands is because he lost the opportunity to earn the additional \$10 wages, not because he earned wages? *Re Pervear*, Fed. Cas. No. 11,053."

§ 2167. Only "Workmen," "Clerks," "Salesmen" or "Servants" Entitled.—The priority is given only to those who were "workmen," "clerks," "salesmen" or "servants" of the bankrupt.⁷⁷

§ 2168. Relationship between Parties Governs and Not Solely Kind of Work.—It is the relationship the claimant bears to the bankrupt, not solely the kind of work, that determines the priority. In other words, the query is not merely: Was the claimant engaged in manual labor? But it is: Did the claimant, when earning the wages, sustain the relation of "workman," "clerk," or "salesman" or "servant" to the bankrupt? If he did, then he is entitled to priority for his services, no matter whether his work were manual work or mental work.⁷⁸ On the other hand, if he did not sustain such relation—if the relationship of master and serving man, master and clerk, or master and workman did not exist—then the claimant is not entitled to priority, no matter if his work were manual work and labor.⁷⁹

Frequently the mistake is made, in preparing proofs of claim for priority claimants, of saying a good deal about "manual work and labor" and

76. *Spruks v. Lackawanna Dairy Co.*, 26 A. B. R. 554, 189 Fed. 287 (D. C. Pa.). Inferentially, *In re B. H. Gladding Co.*, 9 A. B. R. 700, 120 Fed. 709 (D. C. R. I.), where a clerk on his vacation "with pay" was held entitled to priority for the time thus spent on vacation, the wages having been earned.

77. Bankr. Act, § 64 (b) (4); *In re*

Greenberger, 30 A. B. R. 117, 203 Fed. 583 (D. C. N. Y.); *In re Crown Point Brush Co.*, 29 A. B. R. 638, 200 Fed. 882 (D. C. N. Y.). Compare ante, § 47.

78. *Bell v. Arledge*, 27 A. B. R. 773, 192 Fed. 837 (C. C. A. Tex.).

79. *In re Crown Point Brush Co.*, 29 A. B. R. 638, 200 Fed. 882 (D. C. N. Y.).

nothing at all as to whether or not the claimant was a "workman," "clerk," "salesman" or "servant" of the bankrupt.

Thus, a "workman," "clerk," "salesman" or "servant" on vacation "with pay" is nevertheless entitled to priority for the time thus spent on vacation: they are his "wages" and are "earned" already.⁸⁰

In re B. H. Gladding Co., 9 A. B. R. 700, 120 Fed. 709 (D. C. R. I.): "Wages are 'earned' in the sense in which that term is used in the Bankruptcy Act, so long as a bona fide contract of hiring exists, and the clerk or servant continues in the master's employment and does all he is required to do."

And it was held in one case, that the claims of the wife and daughter of a bankrupt should be allowed for services rendered in his store under an express contract.⁸¹

§ 2169. "Workman," "Clerk," "Salesman" and "Servant" to Be Given Ordinary, Popular Meaning.—The words workman, clerk, salesman and servant are to be given their common, everyday, popular meaning.⁸²

In re Smith, 11 A. B. R. 646 (Ref. R. I.): "As used in this section (64) of the Bankruptcy Act it has its popular meaning, namely, 'payment for services rendered, especially the pay of manual laborers receiving a fixed sum per day, week or month,' Standard Dict. 2026, definition 'wage.'"

"See; also, Cyc. Law Dict., definition 'wages.' 'Compensation given to a hired person for manual or other inferior services.'"

In re Grubbs-Wiley Grocery Co., 2 A. B. R. 444, 96 Fed. 183 (D. C. Mo.): "The term 'workmen or servants' is to be presumed to have been employed in its ordinary acceptance. Ordinarily a workman is understood to be 'One who labors; one who is employed to do business for another; a worker; one who is employed in labor.' Doubtless the statute has reference to a workman employed on some character of work—laboring for some person who sustains to him the relation of an employer or master, for whom he works. So, also, the term 'servant' ordinarily means a person employed by another to render personal services to the employer, between whom the relation of master and servant exists, as understood in law."

In re Carolina Cooperage Co., 3 A. B. R. 157, 96 Fed. 950 (D. C. N. Car.): "The class to whom it was evidently the intention of Congress to give priority is that class who labor and serve; parties who, under the laws of some State would have a lien, or at least be preferred to other creditors in the settlement of an estate."

The technical meaning of "servant," as being any one employed by another (as used in the law of personal injury or of master and servant), is broader than its meaning under § 64 (b) of the Bankruptcy Act.⁸³

In re Smith, 11 A. B. R. 646 (Ref. R. I.): "All the decided cases under this subsection of the law give to the words 'workman, clerk or servant' a somewhat restricted meaning."

⁸⁰. Compare, In re E. B. Lewis Co., 12 A. B. R. 281 (Ref. R. I.).

⁸¹. In re Strauch, 31 A. B. R. 36, 208 Fed. 842 (D. C. Ohio).

⁸². In re Greenewald, 3 A. B. R. 697,

99 Fed. 705 (D. C. Pa.); In re Rose, 1 A. B. R. 68 (Ref. Ohio).

⁸³. In re Greenewald, 3 A. B. R. 696, 698, 99 Fed. 705 (D. C. Pa.); In re Zotti, 23 A. B. R. 607 (Ref. N. Y.).

Thus, while, in the eyes of the law, even a high-salaried officer of a corporation may be its "servant," yet, in bankruptcy distribution, he is not entitled to priority, because that kind of "servant" is not what is meant.⁸⁴

But the mere fact that the claimant is a nominal officer of a bankrupt corporation will not of itself, preclude him from priority rights if, in truth, he was employed, and earned wages, as a servant of such corporation.⁸⁵

[Eng.] *Gordon v. Jennings*, 9 Q. B. Div. 45: "The term 'wages' is not applied to the remuneration of a high or important officer of the State or of a county, for instance, but to that of domestic servants, laborers and persons of similar description."

The statute means by servant, a serving man or woman, as the word is used in everyday life. So, also, with "workman," and with "salesman," and with "clerk."

Under the law of 1867 the priority was given to "house-servants." Obviously, the present law means simply to enlarge the class of servants from "house" servants to all kinds of servants about the premises or person of the bankrupt and his family.⁸⁶ So, also, the law of 1867 gave the priority to "operatives." The present law obviously means to confine the priority to that class of operatives known, commonly, as "workmen."

In *re A. O. Brown & Co.*, 22 A. B. R. 496, 171 Fed. 254 (D. C. N. Y.): "Act 1867, * * * provided that priority should not be given, 'except that wages due from him [the bankrupt] to any operative or clerk or house servant' shall be preferred. Under the present act * * * the words are 'workman, clerk, or servant.' 'Workman' is possibly a wider phrase than 'operative,' and 'servant' is undoubtedly wider than 'house servant;' but the section is obviously copied after the law of 1867."

Similarly, persons selling goods in a store are "clerks" within the meaning of the act, as they also are by popular acceptance.⁸⁷

Obiter, In *re Greenwald*, 3 A. B. R. 696, 99 Fed. 705 (D. C. Pa.): "The scope of these words is to be determined, I think, not exclusively by the lexicographers, but in part, at least, by modern usage, which is continually modifying the content of words and phrases. 'Clerk,' for example, has come to include, not only a subordinate who writes letters or keeps books, but also a salesman in a retail store."

But those selling but not in the store are "salesmen."^{87a}

Musicians, employed at regular wages, to play on the bankrupt's roof garden, have been held entitled to priority as "servants."

In *re Caldwell*, 21 A. B. R. 236, 164 Fed. 515 (D. C. Ark.): "A musician employed by the day, week or month at regular wages, while not a 'menial serv-

⁸⁴. In *re Carolina Cooperage Co.*, 3 A. B. R. 157, 96 Fed. 950 (D. C. N. Car.); In *re Zotti*, 23 A. B. R. 607 (Ref. N. Y.); In *re Crown Point Brush Co.*, 29 A. B. R. 638, 200 Fed. 882 (D. C. N. Y.).

⁸⁵. In *re Swain Co.*, 28 A. B. R. 66, 194 Fed. 749 (D. C. Cal.); In *re*

Roberts Co., 27 A. B. R. 437, 193 Fed. 294 (D. C. Minn.).

⁸⁶. Compare, In *re Rose*, 1 A. B. R. 75 (Ref. Ohio).

⁸⁷. In *re Flick*, 5 A. B. R. 465, 105 Fed. 503 (D. C. Ohio).

^{87a}. See post, § 2170.

ant' in any sense of the word, is still one who labors for the benefit of an employer. He is not in pursuit of an independent calling and is subject to his master's commands and must do as directed. The fact that his work is that of an artist does not deprive him of the benefit which the law intended to give to those working for wages for their living. An artist of the highest class might be employed to do some fresco painting at daily wages. Should the fact that he is an artist deprive him of any rights under that provision of the Bankruptcy Act, although his work is performed as a hired employee? I do not think the intent of Congress was so narrow, but rather that it took the broad view that every laborer, clerk, servant or employee working for wages for the benefit of a master or employer, when such wages furnish the means of his livelihood, and where the relationship of master and servant exists within the well known meaning of the law, shall have priority over ordinary creditors for the sum due him for such services, not to exceed three months' wages. Any other construction would do a great injustice to a large class of wage earners to whom their daily earnings are absolutely necessary for their support and that of their families, an injustice which I am not inclined to assume Congress intended to inflict on them. The priorities provided for by the Bankruptcy Act are remedial and should be liberal rather than strictly construed."

They were entitled to such priority, at any rate, as either workmen or servants.

A bookkeeper is a "clerk" within the meaning of the statute, even though only temporarily employed in adjusting the books and accounts.⁸⁸

§ 2170. "Traveling or City Salesman" Also Entitled to Priority.—Traveling or city salesmen before the Amendment of 1906 were not entitled to priority under § 64 (b) (4);⁸⁹ but were entitled to priority under § 64 (b) (5), if the State law recognized the priority.⁹⁰ But traveling and city salesmen are now entitled to priority, by the Amendment of 1906,⁹¹ but only in bankruptcies wherein the adjudication has occurred since 1906.⁹²

§ 2170½. Though Paid by Commissions.—And the traveling or city salesman may be entitled to such priority even though he receive his compensation by way of commissions and not salary.⁹³

In re New England Thread Co., 20 A. B. R. 47, 158 Fed. 788 (C. C. A. Mass.): "A traveling salesman, as commonly understood, may be defined as a man who travels about the country soliciting orders for goods, which orders are sent to his employer for approval. This is the primary service for which he is employed, and it measures the full extent of his responsibility. He is not employed or au-

⁸⁸. In re Baumblatt, 19 A. B. R. 500, 156 Fed. 423 (D. C. Pa.); (1867) Ex parte Rockett, Fed. Cas. No. 11,977.

⁸⁹. In re Scanlon, 3 A. B. R. 202, 97 Fed. 26 (D. C. Ky.); In re Greenwald, 3 A. B. R. 696, 99 Fed. 705 (D. C. Pa.).
⁹⁰. In re Lawler, 6 A. B. R. 184, 110 Fed. 135 (D. C. Wash.).

⁹¹. In re New England Thread Co., 20 A. B. R. 47, 158 Fed. 788 (C. C. A. Mass.), quoted supra; In re Fink, 20 A. B. R. 897, 163 Fed. 135 (D. C. Pa.).

Compare, In re Metropolitan Jewelry Co., 31 A. B. R. 752, — Fed. — (D. C. N. Y.), where the efforts of the salesman were those of a principal rather than those of an employee.

⁹². In re Photo Engraving Co., 19 A. B. R. 94, 155 Fed. 684 (D. C. N. Y.).

⁹³. In re Fink, 20 A. B. R. 897, 163 Fed. 135 (D. C. Pa.); In re Roebuck Weather Strip and Wire Screen Co., 24 A. B. R. 532, 180 Fed. 497 (D. C. N. Y.).

thorized to fix prices. He cannot pass upon the credit or standing of customers. He does not collect accounts. He is not responsible for the quality, condition, or delivery of the goods. He makes no personal contracts, and he has no other interest in the sales than his compensation for those which are approved by his employer. But, while the field of service and responsibility of traveling salesmen is limited the agreements which they make with their employers vary greatly in such details as the form of compensation, the extent of territory, and in many other particulars. A traveling salesman may be paid a fixed sum per day, week or month, or a yearly salary, or a commission on the amount of goods sold, or both a fixed sum in the form of wages or salary, and, in addition thereto, a commission on the amount of goods sold when the sales exceed a certain amount. The territory assigned to him may be confined to a single city or State, or it may cover many cities or States. Commonly, the employer pays the salesman's expenses, but sometimes, especially if he works for a commission, he pays his own expenses. Sometimes the employer has a list of customers, and the salesman receives a commission upon all orders sent in by those customers. Sometimes he is allotted a certain territory, and he receives a commission upon all sales which are sent in from that territory. In some cases the employer may direct the routes he is to travel, and in other cases the salesman chooses his own routes. Sometimes the salesman sends the orders directly to his employer, and sometimes the customers themselves send in the orders to the employer. We do not think any of these details takes a man out of the category of traveling salesman, because, under all these different arrangements, the service and responsibility of the salesman are substantially limited to the obtaining of orders in a certain territory, and having them sent to his employer. * * * The remaining question is whether the word 'wages' in any way limits the class of traveling salesmen who are included within this provision of the Bankruptcy Act. If this provision had been restricted to 'workmen' and 'servants,' it might perhaps be urged that 'wages' should be construed in its narrow and popular sense as meaning the payment of a fixed sum per day, week, or month for manual labor, or other labor of a menial or mechanical kind. But since this provision also includes 'clerks' and 'traveling or city salesmen,' if we construe 'wages' in this narrow sense we necessarily limit the operation of the statute to those clerks and traveling salesmen who happen to be paid for their services in a particular way; in other words, the question of preference is made to turn upon the mode of payment rather than upon the kind of service rendered. The result would be that a clerk who was paid a fixed sum per day, week, or month, which during the year amounted to \$1,000, would be entitled to a preference, while a clerk who was paid this sum in the form of a yearly salary would be excluded; and, further, a traveling salesman who was paid a fixed sum of \$100 or \$500 a month would be entitled to a preference, while a traveling salesman who only earned from \$30 to \$40 per month in the form of commissions would be excluded. It is plain therefore, that 'wages' must be construed in its broader and more general sense as meaning compensation for services rendered, since to hold otherwise would lead to glaring inconsistencies and manifest injustice."

Even where it is the manufacturer who receives the stated percentage and the solicitor who gets all the profit above that percentage, the manufacturer merely paying the workmen's wages and furnishing the material (the solicitor also selecting workmen to put articles in position subject to the manufacturer's approval and also superintending such workmen), the

solicitor has been entitled to priority,⁹⁴ though such ruling pushes the doctrine to its extreme limit.

And it has been held so, even where he was paid by a percentage of the gross sales of his employer and where he was required to pay the incidental expenses of an office and stenographer, besides.

In *re New England Thread Co.*, 18 A. B. R. 840, 154 Fed. 742 (D. C. R. I.): "There is no apparent reason why a salesman may not be paid for his services as salesman by a per centage of the employer's gross sales, as well as by a per centage of those sales procured by his immediate solicitation. Practically, it is a somewhat difficult matter to determine what orders received by an employer are due to the efforts of an experienced and important salesman like the petitioner. Many of the orders received by the employer might have been a consequence more or less direct of previous efforts of the salesman. If practical men deem it proper that the arrangement for compensation should be based on the entire sales in the salesman's territory, whether they are directly traceable to him or not, we cannot say that compensation of this character is not as strictly compensation for services of the salesman as a fixed salary or a fixed per centage of sales actually traceable to the salesman. It is also suggested that, as the petitioner was under expense for an office and stenographer, it is impossible to apportion his wages from his expenses. The fact that by an arrangement between employer and salesman the salesman is to pay his own expenses cannot lessen the salesman's right to the agreed compensation, where the expenses are fairly incidental to the service to be performed."

§ 2171. Definition of "Wage Earner" in §§ 1 and 4 Not Criterion Here.—The definition of "wage earner," given in § 1 of the act, as being one who "works for wages, salary or hire at a rate of compensation not exceeding \$1,500 a year," has reference to those who may be proceeded against in involuntary bankruptcy, and is not controlling upon the question as to who is entitled to priority of payment of wages out of the estate, as being a workman, clerk, salesman or servant.⁹⁵

In *re Gurewitz*, 10 A. B. R. 350, 121 Fed. 982 (C. C. A. N. Y.): "An element of perplexity has been imported into the discussion by the assumption that the language quoted must be interpreted in the light of the definition of the word 'wage-earner' found in § 1 of the act. Subdivision 27 provides that:

"'Wage-earner' shall mean an individual who works for wages, salary, or hire, at a rate of compensation not exceeding one thousand five hundred dollars per year." 30 Stat. 544 [U. S. Comp. St. 1901, p. 3420].

"It will be observed that the word 'wage-earner' is not used in the subdivision now under consideration. The word used is 'wages,' and no technical definition of this word is found elsewhere in the act, probably because the

⁹⁴ In *re Roebuck Weather Strip & Wire Screen Co.*, 24 A. B. R. 532, 180 Fed. 497 (D. C. N. Y.).

⁹⁵ In *re Scanlon & Co.*, 3 A. B. R. 202, 97 Fed. 26 (D. C. Ky.); In *re Carolina Cooperage Co.*, 3 A. B. R. 154, 96 Fed. 950 (D. C. N. Car.); In *re Smith*, 11 A. B. R. 647 (Ref. R. I.). In *re*

Crown Point Brush Co., 29 A. B. R. 638, 200 Fed. 882 (D. C. N. Y.); contra, In *re Becker & Co.*, 31 A. B. R. 596 (Ref. N. Y.); In *re Joseph A. Hurley*, 29 A. B. R. 567, 204 Fed. 126 (D. C. Minn.). Compare, inferentially contra, In *re Rose*, 1 A. B. R. 73 (Ref. Ohio).

lawmakers concluded that when a word so plain and simple was used, and no further explanation was necessary.

"The reason for a concise definition of 'wage-earner' is made apparent by an examination of § 4b, 30 Stat. 547 (U. S. Comp. St. 1901, p. 3423), which provides that 'any natural person, except a wage-earner or person engaged chiefly in farming or the tillage of the soil * * * may be adjudged an involuntary bankrupt. When a wage-earner was thus excepted from the operation of the involuntary features of the act it became necessary to define with precision the meaning of the term. We are, however, of the opinion, that the definition has no application to the present controversy for the reason that the defined word is not found in § 64b (4) 30 Stat. 563 (U. S. Comp. St. 1901, p. 3447)."

§ 2172. Thus, Independent Contractors Not Entitled.—Independent contract workers are not entitled to priority. Thus, one using his own workshop, machinery and tools, himself working as well as employing helpers, to manufacture cheese and butter, at certain rates, for another, out of milk furnished by that other, is an independent contractor and not entitled to priority.⁹⁶

Likewise, a blacksmith who maintains his own shop and shoes horses for whomsoever may apply, is not entitled to priority, although he himself does work.

Weaver v. Stone & Supply Co., 16 A. B. R. 518 (Ref. Ohio): "The three claimants in this case maintained shops where blacksmithing was done for whomsoever might apply to them for work of that character and for whom they were willing to do the work. The relation of employer and employee does not exist between the person taking tools or horses to a blacksmith shop for the purpose of having blacksmithing done for them and the person doing the work. They are no more employer and employee than are the person taking a watch to a watchmaker and the watchmaker who repairs the watch."

Again, one who buys, at wholesale, from jobbers, as the agent of any one who employs him, and receives a commission from each one for purchases made in that person's behalf, is not entitled to priority.⁹⁷ And, similarly, incidental commissions for getting customers, where the regular employment by the bankrupt is for other services, there being no obligation to serve in getting the customers, does not entitle one to priority for the commissions.⁹⁸

For the same reason factors are not entitled to priority.¹ And a general expressman doing draying for the general public and at the same time doing all of the bankrupt's draying, as ordered, is not entitled to priority.²

Again, one who employs workmen on the premises of the bankrupt to manufacture goods for the bankrupt, under the bankrupt's supervision, even where his workmen are paid by the bankrupt (on his account) is

⁹⁶. In re Rose, 1 A. B. R. 68 (Ref. Ohio).

⁹⁷. In re Smith, 11 A. B. R. 646 (Ref. R. I.).

⁹⁸. In re Mayer, 4 A. B. R. 119, 101 Fed. 227 (D. C. Wis.).

¹. Obiter, In re Smith, 11 A. B. R. 646 (D. C. R. I.).

². Obiter, In re Smith, 11 A. B. R. 646 (D. C. R. I.).

nevertheless an independent contractor and not entitled to priority, where the risk of profit or loss rests upon him by the contract: he is an employer of labor and not a workman, notwithstanding his close relation to the bankrupt.

In re [Thomas] Deutschle & Co. (No. 1), 25 A. B. R. 343, 182 Fed. 430 (D. C. Pa.): "He had charge, no doubt, of the blind department of the bankrupts' factory, but he was not a foreman or head workman so as to bring him within the statute. The relation was peculiar. The men under him were his own, hired and discharged by him, and he was paid for the work which they turned out at so much a piece, and was answerable for it, as for instance, if it was spoiled or not properly finished. This work was done at the factory of the bankrupts with the aid of materials and machinery which the bankrupts furnished, but was none the less that of the claimant, the men working for him and under his direction in making blinds, which he had contracted for. When they went outside of this, to do work for the bankrupts, the claimant was entitled to a cent an hour advance on the wages that he paid them; and he was charged the same amount when any of the bankrupts' men were called upon to assist him. The bankrupts, it may be, supervised it all and at times gave directions. And the hours of the men were regulated by the shop whistle, just as their wages were taken care of by the bankrupts for the claimant on pay-day. The blind department, also as so organized, was a part of the general establishment. But the fact remains, that the claim presented here, for which priority is asked, arises out of a contract with the bankrupts by which the claimant agreed to put out certain work for a certain price, furnishing his own men, and getting the benefit of their labor. The labor done was not his, but that of his men, however he may have, in a general way participated in it; and he profited according as he managed to get good work out of them. In this he was not a workman or laborer, but an employer of labor, and the remuneration to which he was entitled was not wages, but an agreed price for articles produced, which the law does not undertake to preferentially provide for."

But an ordinary day laborer, who does work with his hands, lifting logs, plowing, etc., has been held to be a "wage earner" *exempt from bankruptcy* although he works for different people, and at irregular intervals and owns the team that is used by him in the work.

Analogously, In re Yoder, 11 A. B. R. 445, 127 Fed. 894 (D. C. Pa.): "Upon these facts I think it is clear that the bankrupt was a wage earner and not an independent contractor. He was a servant hired by successive masters, and was always paid by the day, never by the job. The fact that he used his horses and wagons in performing the services for which he was paid by the day does not seem to me of any special importance. A carpenter, or any other skilled mechanic, employs tools—often his own tools—to assist him in earning his daily wages, and the bankrupt's horses and wagons stand, I think, in precisely the same category. * * * He was not an independent contractor, looking for his income to the profits that he might make by carrying out a contract for a lump sum, but was an ordinary day laborer, who did work with his hands, lifting logs, holding a plow, driving his team and similar services for which he was paid at a fixed rate by the day."

And it has been held that the reasonable value of a teamster's own services may be separated from that of the use of his team and wagon, and

priority be given for the services and denied for the use of the team and wagon, although the contract be for both together without separation." Such rule is of doubtful authority. With quite as good reason could the value of the individual services of the various independent contractors in the above instance be separated by estimate from that of their employees.

§ 2173. Exclusive Employment by One Person Not Requisite.—Exclusive employment by one person may not be taken as a requisite.⁴

§ 2174. But Employment by Several Tends to Show Independent Contractor.—Yet employment by a large number goes far to show that an employee is an independent contractor rather than a servant.⁵

§ 2175. "Piece Workers" May Be Entitled.—Piece workers may be entitled to priority as "workmen." There is nothing in the mere manner of payment by the piece to prevent such workers coming within the meaning of the term workmen.⁶

§ 2176. Idea of Subordination Implied.—The idea of subordination is implied.⁷

In re Gurewitz, 10 A. B. R. 351, 121 Fed. 982 (C. C. A. N. Y.): "The legislative intent * * * is manifest. It is to give a preference, limited in time and amount, to those employees of the bankrupt who work for wages. It surely could not have been the purpose of Congress to make the method of computation a criterion of priority. There is absolutely nothing in the language quoted, upon which to base such an assumption. In order to secure priority under this subdivision, the creditor must establish the following facts: First, that he was a workman, clerk or servant of the bankrupt. Second, that he earned wages within three months prior to the commencement of the proceedings.

"There is nothing ambiguous about the use of the word 'wages' in this connection. It means the agreed compensation for services rendered by the workmen, clerks or servants of the bankrupt—those who have served him in a subordinate or menial capacity and who are supposed to be dependent upon their earnings for their present support. Whether their employer has agreed to pay

3. In re Lumber Co., 17 A. B. R. 117 (D. C. Ky.): But this case comes close to the border line of independent contract. To be sure the mere furnishing of the tools by the workmen will not prevent his claim being that of a "workman," within § 64 (b) (4); but on the other hand the furnishing of a horse and wagon under an entire contract including his own services comes very close to being an independent contract relation rather than that of a subordinate "workman."

4. In re Smith, 11 A. B. R. 648 (Ref. R. I.); analogously, In re Yoder, 11 A. B. R. 445, 127 Fed. 894 (D. C. Pa.); instance, In re National Marble & Granite Co., 31 A. B. R. 80, 206 Fed. 185 (D. C. Ga.).

5. In re Smith, 11 A. B. R. 646 (Ref. R. I.).

6. In re Rose, 1 A. B. R. 76 (Ref. Ohio); obiter, *Weaver v. Hugill Stone & Supply Co.*, 16 A. B. R. 517 (Ref. Ohio). Obiter, In re Gurewitz, 10 A. B. R. 351, 121 Fed. 982 (C. C. A. N. Y.), quoted at § 2176.

7. In re Rose, 1 A. B. R. 73 (Ref. Ohio); inferentially, In re Grubbs-Wiley Grocery Co., 2 A. B. R. 442, 96 Fed. 183 (D. C. Mo.); *Weaver v. Hugill Stone & Supply Co.*, 16 A. B. R. 516 (Ref. Ohio); In re Zotti, 23 A. B. R. 607 (Ref. N. Y.); In re Greenberger, 30 A. B. R. 117, 203 Fed. 583 (D. C. N. Y.).

them by the hour, the day, the week the month or by the 'job' or piece, is wholly immaterial.

"It is incredible to suppose that Congress intended to discriminate against the vast army of laborers who, in the coal mines, the foundries, the clothing manufactories and in almost every branch of industry, are paid, not according to the time consumed, but according to the work accomplished."

In *re Smith*, 11 A. B. R. 646 (D. C. R. I.): "The purpose of the law seems to have been to protect subordinate helpers or assistants and to pay in full those dependent on their wages as means of a livelihood. The meaning of 'wages' * * * carries with it the idea of subordination."

In *re Greenwald*, 3 A. B. R. 697, 99 Fed. 705 (D. C. Pa.): "The essential idea conveyed by this word, as commonly used, is the idea of a subordinate, whose occupation has nothing to do with correspondence or books of account, but requires him to use his hands to a considerable degree in manufacturing or building, or in similar pursuits. He may be skilled or unskilled; he may or may not, be aided by tools or machinery; but he does not belong to the same class as the man that is neither making goods nor erecting buildings, nor accomplishing similar results, but is exclusively engaged in the sale of a finished product."

In *re Greenberger*, 30 A. B. R. 117, 203 Fed. 583 (D. C. N. Y.): "It can make no material difference that Greenberger was carrying on this business as an individual. The fact that, as incident to the performance of his duties as general manager of this store, he kept it clean and did some clerical duty does not change the character of his employment. He was not employed to do that work, but to manage the business, and he was paid for managing it, and not for performing such menial service as he did perform as incident to the management. The claim is for salary and for salary as manager, not for services as a clerk or general workman and compensation as such. The referee was right in holding that the claim of Cohen could not be allowed as one entitled to priority. It would hardly do to hold that the general manager of the business of a corporation or individual, employed and paid as such, becomes entitled to priority, for the reason he incidentally sweeps the floor, dusts the counters, and assists in selling goods."

In *re Crown Point Brush Co.*, 29 A. B. R. 638, 200 Fed. 882 (D. C. N. Y.): "There can be no pretense that these debts, or either of them, was entitled to priority of payment under any law or statute of the State of New York if not so entitled under the provisions of the Bankruptcy Act. Clearly the president and general manager of a corporation is not a clerk or a traveling or city salesman, even though he may incidentally and occasionally do some clerical work, or perform some clerical duties, or make some sales. The same may be said of the treasurer and assistant general manager of a corporation, even though the treasurer keeps his own books and makes his own entries. The duties of a 'general manager' and of an 'assistant general manager' are to manage, control, direct, guide the business; see that it is carried on pursuant to the policy or directions of the board of directors. If it should appear that a corporation employs a clerk to do or perform clerical duties at a fixed compensation or salary, and also empowers him to exercise certain powers of direction, supervision, and control or management, without added or extra compensation, he would be a clerk, within the meaning of the law, and his claim for salary would be entitled to priority; but should it employ him as clerk to perform clerical duties and set him to perform the duties of general or assistant general manager, and have the clerical duties performed by others he would not be a clerk, and his wages would not be due to a clerk, but to a general man-

ager, or to an assistant general manager, as the case should be. The law would not tolerate an evasion of that kind. Wages due the general manager of a business or corporation are not entitled to priority of payment. On the other hand, should a corporation employ a person to act as and perform the duties of general manager or assistant general manager at a fixed salary and, finding such services unnecessary, set him to perform the duties of clerk, floor sweeper, and furnace tender, he would be, in fact, either a workman or a servant, within the meaning of the law, and his claim for salary so earned would be entitled to priority. He would have the right to accept the inferior employment and perform its duties. But should he voluntarily, while holding the position of assistant general manager, perform manual labor assigned as part of his duty, he would not become a workman or servant, and entitled to priority. His character would be determined by what he was employed to do. Here, as assistant general manager, John Morrison, Jr., was to perform such duties as the general manager shall prescribe. In a sense all employees of a corporation, from president down, are 'workmen' or 'servants.' They work, and they serve."

Thus, managing officers are not entitled to priority.⁸

In *re Grubbs-Wiley Grocery Co.*, 2 A. B. R. 444, 96 Fed. 183 (D. C. Mo.): "This claimant was himself a stockholder in this corporation, and was one of the board of directors, and was its general manager. As such general manager he stood in the relation of vice-principal of the corporation. * * * Could it be maintained that he was a workman or servant of the company on a salary, entitling him, on the declaration of bankruptcy of the concern, to have his salary paid as a preferred claim? Indeed, it would present a remarkable feature of the Bankrupt Act, if the managing officers of a business corporation could vote themselves salaries ad libitum, and after, by their mismanagement, wrecking the company, and inviting an adjudication of bankruptcy, they could, to the exclusion of other creditors of the concern, whose money and property they had obtained on credit, come in as preferred creditors, to the exclusion of such general creditors. The act, in my judgment, admits of no such construction."

In *re A. O. Brown & Co.*, 22 A. B. R. 496, 171 Fed. 254 (D. C. N. Y.): "It is quite clear that Olmsted is not a 'workman' for the bankrupt. Nor is he a 'servant,' because the term does not include all instances of the formal relation of master and servant. * * * The only thing left that he could be, therefore, is a 'clerk.' No one would think of calling the manager in charge of the Chicago branch of a broker's office a 'clerk'—he himself least of all. Whether or not he is employed for 'wages,' he is much distinguished from a clerk."

But compare, In *re New Eng. Thread Co.*, 20 A. B. R. 47, 158 Fed. 788 (C. C. A. Mass.): "There is a general argument of some force which has been brought to our attention against any construction of this provision which would include the present claimant. This argument is that Congress intended by this provision to carry out the policy of the law of giving a preference to those who serve in a subordinate or menial capacity, and who are therefore presumed to be dependent upon their earnings for their present support; and, such being the intention of Congress, this provision should not be held to cover the case of a man who earns \$4,000 a year as commissions for selling goods. While this argument is plausible, it will not bear analysis. Had

8. In *re Carolina Cooperage Co.*, 3 A. B. R. 154, 96 Fed. 950 (D. C. N. Car.); [Eng.] *Gordon v. Jennings*, 9 Q. B. Div. 45; In *re Metropolitan Jewelry Co.*, 31 A. B. R. 752, — Fed. — (D. C. N. Y.); In *re Greenberger*, 30 A. B. R. A. 117, 203 Fed. 583 (D. C. N. Y.).

Congress intended to give a preference only to a subordinate class of clerks and traveling salesmen, it should have so framed the statute as to limit the preference to clerks and traveling salesmen who received a comparatively small compensation for their services, and should not have used language which applies equally to all classes of clerks and traveling salesmen, without regard to the amount of their remuneration."

Thus, similarly, the editor of a bankrupt newspaper is not entitled to priority.⁹

But where claimant was merely a "dummy" director and secretary of the bankrupt corporation, serving as a matter of accommodation to the real owner, his claim for wages earned as steward in the restaurant of the bankrupt is entitled to priority.¹⁰

§ 2177. Correlative Obligation to Serve Implied.—The mere obligation to pay one for whatever service he might do, with no obligation upon him to perform any services, will not entitle such one to priority.¹¹

§ 2178. Must Be Performed within Three Months before Bankruptcy.—The services must have been performed within three months preceding the filing of the bankruptcy petition, in order to claim priority under § 64 (b) (4).¹²

Thus, where the priority claimant has suffered his employer, the bankrupt, to retain a portion of his wages as they have been earned, to accumulate a fund with which to go to college, the priority claim could not cover this amount;¹³ although, presumably, if the precise money so retained could be traced into any particular fund, it might be reclaimed as a trust fund.

§ 2179. Whether May Be for Services Covering Longer Period if Priority Claimed Not under § 64 (b) (4) but under § 64 (b) (5).—But perhaps it may be for a longer period if priority is not claimed under § 64 (b) (4) but is claimed under § 64 (b) (5) where such priority is given by the state statute for a longer period.¹⁴

However, by the weight of authority it is held that where the state prior-

9. In re Zotti, 23 A. B. R. 607 (Ref. N. Y.).

10. In re Swain Co., 28 A. B. R. 66, 194 Fed. 749 (D. C. Calif.). See, also, where priority allowed to bookkeeper who was elected a "nominal" director and treasurer, but continued her ordinary duties as bookkeeper. In re Roberts Co., 27 A. B. R. 437, 193 Fed. 294 (D. C. Minn.).

11. In re Mayer, 4 A. B. R. 119, 101 Fed. 227 (D. C. Wis.).

12. In re Rouse, Hazard & Co., 1 A. B. R. 234, 91 Fed. 96 (C. C. A. Ills.); In re Slomka, 9 A. B. R. 635, 122 Fed. 630 (C. C. A. N. Y.); In re Huntensburg, 18 A. B. R. 697, 153 Fed. 768 (D.

C. N. Y.); In re Van Wert Machine Co., 26 A. B. R. 597, 186 Fed. 607 (D. C. Mass.); In re Dunn, 25 A. B. R. 103, 181 Fed. 701 (D. C. N. Y.). Compare In re National Marble & Granite Co., 31 A. B. R. 80, 206 Fed. 185 (D. C. Ga.).

13. In re Flick, 5 A. B. R. 465, 105 Fed. 503 (D. C. Ohio).

14. In re Lawler, 6 A. B. R. 184, 110 Fed. 135 (D. C. Wash.); In re Gerson, 1 A. B. R. 251 (Ref. Penna.); inferentially, In re Laird, 6 A. B. R. 1, 109 Fed. 550 (C. C. A. Ohio). Compare, obiter, inferentially, In re Yoke Vitrified Brick Co., 25 A. B. R. 18, 180 Fed. 235 (D. C. Kan.).

ity covers the same class covered by § 64 (b) (4) of the Bankruptcy Act, the only claim that may be made must be under § 64 (b) (4).¹⁵

In *re Slomka*, 9 A. B. R. 635, 122 Fed. 630 (C. C. A. N. Y.): "If by the State law the debts were within the general description of clause 5, we are of opinion that the clause would not apply and that the terms of clause 4 supply the exclusive rule for determining what debts for wages are entitled to priority. No principle of statutory construction is better settled than that which displaces the application of general provisions to a particular subject when there are specific provisions applicable to it in the same act. The subject of claims for wages is specifically regulated by clause 4, and its provisions express the particular intent of Congress regarding priority of such claims. As these confine the priority to wages earned within the three months before the commencement of the bankruptcy proceedings, debts like the present are not included. We agree upon this question with the decision of the Circuit Court of Appeals for the Seventh Circuit, In *re Rouse, Hazard & Co.*, 1 A. B. R. 234, 91 Fed. Rep. 96, and for the reasons which are so satisfactorily stated in the opinion in that case. We have given due consideration to the decision by the Circuit Court of Appeals for the Sixth Circuit, In *re Laird*, 6 Am. B. R. 1, 109 Fed. 550, but we are unable to regard it as correct."

Of course § 64 (b) (5) would apply and might, if the state statute so provided, cover services rendered before the three months, if the claimants were not "workmen," "clerks" nor "servants."

§ 2179¹/₂. Application of Payments to Wages Earned before Three Months.—The ordinary rules as to the rights of parties in the application of payments apply; thus, where part of the unpaid wages were earned before the three months period and part within that period the claimant is at liberty to apply the payments on the unpaid wages not entitled to priority in the absence of previous application by the bankrupt.¹⁶

§ 2180. Not to Exceed "Three Hundred Dollars."—No more than three hundred dollars may be allowed as a priority claim to any one claimant under § 64 (b) (4).

§ 2181. But Perhaps for More if Priority Claimed Not under § 64 (b) (4) but under § 64 (b) (5).—But perhaps more may be allowed, if the state statute so provides, where the claim is made under § 64 (b) (5);¹⁷ at any rate, where the claimant is not strictly a "workman," "clerk," "traveling or city salesman," nor "servant" within the classification of the Bankrupt Act.

15. In *re Rouse, Hazard & Co.*, 1 A. B. R. 234, 91 Fed. 96 (C. C. A. Ills.); In *re Crown Point Brush Co.*, 29 A. B. R. 638, 200 Fed. 882 (D. C. N. Y.). Compare, § 2203. Contra, In *re Laird*, 6 A. B. R. 1, 109 Fed. 550 (C. C. A. Ohio). See post, §§ 2194, 2203.

No priority to infant's wages (not within § 64 (b) (4) on theory that contract of employment repudiated gives right of return of proceeds of

labor. In *re Huntenberg*, 18 A. B. R. 698, 153 Fed. 768 (D. C. N. Y.).

16. In *re Andrews*, 19 A. B. R. 441 (Ref. N. Car.); compare, In *re McIntyre Bros.*, 21 A. B. R. 588 (Ref. Miss.) Also, see ante, § 1189. But compare, In *re Flick*, 5 A. B. R. 465, 105 Fed. 503 (Ref. Ohio).

17. In *re Lawler*, 6 A. B. R. 184, 110 Fed. 135 (D. C. Vt.).

§ 2182. Reducing Claim to Judgment, Not Such Merger as to Lose Priority.—The claim of a workman, clerk, traveling or city salesman, or servant reduced to judgment is not so far merged in the judgment as to lose the priority originally attached thereto.¹⁸

§ 2183. Nor Is Priority Lost by Assignment of Claim.—Workmen's, clerks' and servants' claims, assigned to a third party after the filing of the bankruptcy petition, do not lose their priority, and the assignee has the same priority the workmen, clerks, traveling or city salesmen, and servants themselves would have had.¹⁹

A fortiori (even where assigned before the filing), *In re Harman*, 11 A. B. R. 64, 128 Fed. 170 (D. C. W. Va.): "I am of opinion that the Bankruptcy Act was intended by Congress to prefer claims for labor performed within three months prior to the filing of the petition regardless of the fact that they may have been assigned. And I think this is indicated by the use of the word 'claimant' instead of 'workman' in § 64."

Nor is priority lost even if the wages claims be assigned before the filing of the petition.²⁰

Shropshire, Woodliff & Co. v. Bush, 17 A. R. R. 79, 204 U. S. 186: "The precise inquiry is whether the right of prior payment thus conferred is attached to the person or to the claim of the wage earner; if to the person, it is available only to him, if to the claim it passes with the transfer to the assignee. In support of the proposition that the right is personal to the wage earner, and enforceable only by him, it is argued that it is not wages earned within the prescribed time which are given priority, but wages 'due to workmen, clerks or servants;' that where the claim is assigned to another it is no longer 'due to workmen, clerks or servants,' but to the assignee, and therefore when presented by him lacks one of the characteristics which the law makes essential to priority. In this argument it is assumed that the wages must be 'due' to the earner at the time of the presentment of the claim for proof, or at least at the time of the commencement of the proceedings in bankruptcy. Without that assumption the argument fails to support the conclusion. But the statute lends no countenance to this assumption. It nowhere expressly or by fair implication says that the wages must be due to the earner at the time of the presentment of

18. *In re Anson*, 4 A. B. R. 231, 101 Fed. 698 (D. C. Calif.); compare, *In re McBryde*, 3 A. B. R. 729, 99 Fed. 686 (D. C. N. Car.); compare, *In re Johnson*, footnote to 4 A. B. R. 231 (D. C. Calif.).

19. A fortiori (even where assigned before the filing), *Shropshire, Woodliff & Co. v. Bush*, 17 A. B. R. 79, 204 U. S. 186; *In re Campbell*, 4 A. B. R. 535, 102 Fed. 686 (D. C. Wis.); [1867] *In re Brown*, 4 Ben. 142, Fed. Cases No. 1,974; obiter, *In re North Carolina Car Co.*, 11 A. B. R. 488, 127 Fed. 178 (D. C. N. Car.). Compare, same rule as to priorities under Bankr. Act, § 64 (b) (5). *In re Bennett*, 18 A. B. R. 320, 153 Fed. 673 (C. C. A. Ky.). Compare, however, post, § 2279. On the facts,

In re Yoke Vitrified Brick Co., 25 A. B. R. 18, 180 Fed. 235 (D. C. Kans.).

20. *In re Harmon*, 11 A. B. R. 64, 128 Fed. 170 (D. C. W. Va.). Contra, *In re Ice Mfg. & Storage Co.*, 17 A. B. R. 194 (D. C. Mo.). Also, contra, obiter *In re North Carolina Car Co.*, 11 A. B. R. 488, 127 Fed. 178 (D. C. N. Car.). Obiter, *United Surety Co. v. Iowa Mfg. Co.*, 24 A. B. R. 726, 179 Fed. 55 (C. C. A. Mo.).

It has been held that the assignment must have been made in "good faith." *Bell v. Arledge*, 27 A. B. R. 773, 192 Fed. 837 (C. C. A. Tex.). But these queries arise: "Good faith" towards whom? And what is the difference so long as the original claim itself is justly entitled to priority?

the claim, or of the beginning of the proceedings, and we find no warrant for supplying such a restriction. Regarding, then, the plain words of the statute, and no more, they seem to be merely descriptive of the nature of the debt to which priority is given. When one has incurred a debt for wages due to workmen, clerks or servants that debt, within the limits of time and amount prescribed by the Act, is entitled to priority of payment. The priority is attached to the debt and not to the person of the creditor; to the claim and not to the claimant. The Act does not enumerate classes of creditors and confer upon them the privilege of priority in payment, but, on the other hand, enumerates classes of debts as 'the debts to have priority.'"

Obiter, In re Fuller & Bennett, 18 A. B. R. 443, 152 Fed. 538 (D. C. W. Va.): "That § 64b of the Bankrupt Act was designed to protect the wage-earner, dependent for his living upon his daily wage, cannot be questioned. That it gave a preferential lien for the wages earned three months prior to the bankruptcy proceeding, without requiring notice by recordation or otherwise, of such lien, is also true. Common experience tells us that laboring men, owing to their financial exigencies, constantly find it necessary in some way to forestall the securing the benefit of their wages prior to the time fixed for them to become due and payable by their employers. Thus, nothing is more common than for them to secure a certificate of some kind or form, showing that they have earned or are entitled to a sum for such wages, which they can assign to another and thereby secure money or supplies necessary for their immediate needs. To say that a person cannot take an assignment of such wages without losing the lien which the laborer by law clearly has, would in very many cases militate against the interests of the laborer and not in his favor. It would in many cases cause him to sell such demands at ruinous discounts. Certainly this was exactly the opposite of the humane purpose of the statute. To say that he may, after proving his claim for wages in the bankruptcy proceeding, which necessarily causes delay, assign it and preserve the lien to the assignor, but cannot do so before such proof in bankruptcy or before bankruptcy proceeding commenced against his employer, seems to me to be a narrow and technical construction, not warranted. Suppose his claim be wholly undisputed and admitted; what possible reason is there why he should be required to either starve or suffer, awaiting the law's delays, before realizing, by assignment, upon it? Both before and after proof in bankruptcy, it is the claim for the same labor performed, and supported by the same equities, and in either case he has derived the same relief from the assignment. It therefore seems to me that one who takes by assignment from a wage-earner such claim, who has in this way aided and relieved the wage-earner in realizing without delay the means required by his necessities, ought not to be in a sense discriminated against and punished for so doing. Therefore it seems to me that the assignee of such labor claim who presents it as such, in its original form and subject to its original equities, should be held to take by such assignment all the rights of the assignor, including the right to preference given by this § 64b."

Contra, In re Westlund, 3 A. B. R. 646, 99 Fed. 399 (D. C. Minn.): "This language requires that a debt for wages, to have priority, must be due to the wage earner. If the claimant entitled to priority might be an assignee, there would be no reason why such claimant should be restricted to \$300, as he might be the owner of many small claims, each less than that amount, but aggregating more. The clause referred to is intended to favor the class whose reliance for the maintenance of themselves and families is generally upon their wages, as earned. There is nothing in the nature of security or lien for the payment of the wages which could pass to an assignee. No right to priority arises or

exists until the proceeding in bankruptcy is instituted, and then the wages assigned are not 'due to workmen, clerks or servants,' but to their assignees, and are outside the language of this clause. If debts for wages so assigned can be allowed priority, they may come in conflict, or at least in competition, with other claims for wages due and owing to the same workmen, clerks and servants, earned within the same three months, and lessen the payments, if the assets will not pay in full all debts having priority. It must be held, therefore, that debts of a bankrupt for labor and services which at the commencement of the proceedings in bankruptcy are not due to the workmen, clerks or servants, but to assignees, have no priority."

§ 2183½. Whether Priority Lost by Assignee's Acceptance of Note.—It has been held, however, that such priority is lost by the assignee's acceptance of new obligations payable to the assignee himself, or where the assignee otherwise novates the debt or merges it with other debts; thus, as to the acceptance of a new promissory note.

In *re Fuller & Bennett*, 18 A. B. R. 443, 152 Fed. 538 (D. C. W. Va.): "But this [the principle of § 2183, ante], it seems to me, should always be subject to this important condition and limitation: That, after having so acquired by assignment he must not novate the debt nor merge it with other debts, or take from the debtor new obligations and securities therefor wholly due and payable to himself. It is not to be forgotten that the liens of this kind are not recorded, and the outside creditors can obtain no notice of them in that way. When presented in their original form, either by the wage-earner or by his assignee, it is easy enough for other creditors to ascertain whether the claim is just and comes within the limits of the statute; but on the other hand, suppose one takes by assignment from say 50 or 100 different laborers their several claims and merges them together and secures from the employer a new obligation for the total amounts, made to himself, does he not novate the debt?"

Yet, referring to the court's opinion in *Re Fuller & Bennett*, the question of the waiver of the priority is largely a question of intent, as shown by the facts; whilst difficulties in the way of verifying the propriety of the various claims should not be erected into a rule of law that an assignment to one by several or many deprives the claims assigned of the priority which they would have retained had they been assigned each to a different assignee.

And the salutary rules enunciated in the next paragraph, § 2184, regarding equitable subrogation of parties advancing moneys to meet pay rolls, should not be lightly thrown aside.

§ 2184. Subrogation of Persons Advancing Money to Meet Pay Rolls.—Persons advancing money to bankrupts to meet pay rolls, under agreement that such pay rolls should be assigned, probably may be subrogated to the rights of the workmen thus paid. This would be nothing more than the application of the rule of equitable subrogation.²¹

²¹. But contra, if the pay rolls were not in fact assigned, In *re North Carolina Car Co.*, 11 A. B. R. 488, 127 Fed. 178 (D. C. N. Car.); but this is not

correct, for the advancement under the agreement creates the equity whether carried out or not unless the assignment was actually waived. See post,

Likewise, probably, if such advancement be made to preserve the business by one interested therein.

Yet there is considerable doubt as to the applicability of the doctrine of subrogation—whether it be subrogation by agreement or by force of equity—to wages claims before the bankruptcy.

And it would seem at any rate that such assigned claims should not compete for priority with the claims still owned by workmen, clerks, traveling or city salesmen or servants.²²

§ 2185. **Due "Proof" to Be Made of Priority Claim.**—Due proof of claim must be filed. It is none the less a "provable debt" requiring due "proof" before payment because of being a priority debt.²³

§ 2186. **Wages Claims "of Workmen, Clerks, Traveling or City Salesmen and Servants" No Precedence over Valid Prior Liens.**—Priority claims for wages of workmen, clerks, traveling or city salesmen or servants under the bankruptcy classification do not have precedence over valid liens in the distribution of assets covered partly or wholly by liens.²⁴ However, of course where by state law certain wages claims have such precedence, they will preserve their precedence in bankruptcy;²⁵ although such precedence will result not from § 64 (b) (4) but rather from § 64 (b) (5).

But it has been held that even if by state law such priorities would have precedence over prior valid liens yet, in bankruptcy, such prior liens are protected by § 67 (d).

In re Yoke Vitriified Brick Co., 25 A. B. R. 18, 180 Fed. 235 (D. C. Kans.): "The question presented for decision is this: Are petitioners entitled to be paid out of the money now in the hands of the trustee in bankruptcy awaiting distribution which arose from a sale of the property under the order of court,

"Subrogation to Rights of Various Parties in Distribution of Assets," Division 5. Compare, *Bell v. Arledge*, 28 A. B. R. 773, 192 Fed. 837 (C. C. A. Tex.). But compare doubtful ruling in *United Surety Co. v. Iowa Mfg. Co.*, 24 A. B. R. 726, 179 Fed. 55 (C. C. A. Mo.), discussed in note to § 2191.

22. See post, "Whether Subrogation to Workmen's Priority Claims to Compete with Workmen's Own Later Claims," § 2279.

23. See ante, this chapter, § 2138. In re Dunn, 25 A. B. R. 103, 181 Fed. 701 (D. C. N. Y.).

24. In re Mulhauser, 10 A. B. R. 231, 121 Fed. 669 (C. C. A. Ohio); In re Frick, 1 A. B. R. 719 (Ref. Ohio.). Compare same rule under state priority, In re Falls City Shirt Mfg. Co., 3 A. B. R. 437, 98 Fed. 592 (D. C. Ky.); contra, In re Erie Lumber Co., 17 A. B. R. 699 (D. C. Ga.); In re Proudfoot, 23 A. B. R. 106, 173 Fed. 733 (D. C. W.

Va.); In re Allert, 23 A. B. R. 101, 173 Fed. 691 (D. C. N. Y.). Compare, *Smith v. Motley*, 17 A. B. R. 865, 150 Fed. 266 (C. C. A. Ohio). Contra, In re McDavid Lumber Co., 27 A. B. R. 59, 190 Fed. 97 (D. C. Fla.).

It has been held, that where, after a fraudulent conveyance by way of note and mortgage has been set aside, the payee of the note sets up that the note was for wages and claims priority, this claim for priority, being still based on the fraudulent note, will be rejected. In re Hemstreet, 14 A. B. R. 823, 139 Fed. 958 (D. C. Iowa): "It is possible that there is due some amount, as wages, from the bankrupt; but as the claimant has rested his claim upon the notes and mortgage he must abide the conclusion thereon, and they being invalid, he is not entitled to other relief against the creditors."

25. In re Byrne, 3 A. B. R. 268, 97 Fed. 762 (D. C. Iowa); In re Erie Lumber Co., 17 A. B. R. 699 (D. C. Ga.).

freed from liens thereon, in preference to the demands of those having fixed and valid liens on the property at the date of the adjudication?

"In so far as the statute of the State above quoted is concerned, it may be said: Conceding for the purpose of argument, as contended by petitioners, the broad and comprehensive language of the statute should be held to grant to the laborers and employees therein enumerated a prior right of payment to those having fixed liens on the property of an insolvent in the hands of a receiver or assignee for the benefit of creditors, if that question were presented in other than a bankruptcy proceeding, and further conceding this proceeding in bankruptcy is the legal equivalent for the receivership or assignment for the benefit of creditors employed in the statutes, as I think must be done (see *In re Laird* (C. C. A., 6th Cir.), 6 Am. B. R. 1, 109 Fed. 550, 48 C. C. A. 538), yet the question remains: Does it follow therefrom petitioners are entitled to be paid out of the fund now in the hands of the trustee in this case, in preference to the rights of the mortgagee and mechanics' lien claimants here opposing such payment?

"I think not, and for the following reasons: The liens here asserted are admittedly valid and within the protection afforded by § 67d of the Bankruptcy Act. Therefore the mandate of the act is: Such liens shall not be affected by the provisions of the act; that is to say, neither the priority nor the validity nor any other subsisting right in the property acquired and held by virtue of such liens shall be affected by any provision of the Act."

DIVISION 3.

PRIORITIES UNDER FEDERAL AND STATE LAW.

§ 2187. **Priorities Granted by State and Federal Laws.**—The last class of claims entitled to payment before general creditors are debts owing to any person who, by the laws of the States, or of the United States, is entitled to priority.²⁶

Such claims must not only be entitled to priority under state law but also, of course, be provable under the provisions of the Bankruptcy Act, in order to be entitled to priority.²⁷

The State priorities, of course, are not priorities over all other claims whatsoever but only over those that are not specified in § 64 of the Bankruptcy Act as being higher in right.²⁸

§ 2188. **"Priority" to Be Distinguished from "Liens."**—Priority here does not refer to liens existing on the bankrupt's property nor to the order of payment of such liens, but to the order of payment out of the general assets of an insolvent's estate on distribution.²⁹

In re Cramond, 17 A. B. R. 38, 145 Fed. 966 (D. C. N. Y.): "It may be well to remark that in my opinion subdivision 5 of § 64 of the Bankruptcy Act has no reference to liens actually existing at the time of the adjudication. Liens on the property of the bankrupt, not void or voidable under some provisions of the law, whether

²⁶ Bankr. Act. § 64 (5). *In re Chaudron & Peyton*, 24 A. B. R. 811, 180 Fed. 841 (D. C. Md.).

²⁷ *In re Sterne & Levi*, 26 A. B. R. 535, 190 Fed. 70 (D. C. Tex.).

²⁸ *In re Consumers' Coffee Co.*, 18 A. B. R. 500, 151 Fed. 933 (D. C. Pa.).

²⁹ Compare, post, § 2205.

obtained and created by express contract or by virtue of compliance with the lien law of a State, since the amendment to the Act, are first to be paid, excepting taxes subject to abatement for commissions expressly allowed to referees and trustees on all sums disbursed to creditors in the one case and to any one in the other. While all liens are, in a sense, priorities, and certain priorities may be liens, in a sense, still all priorities are not liens, and, in my opinion, clause 5 of subdivision b of § 64 does not refer, and was not intended to refer to liens on the estate of the bankrupt. It was assumed that valid liens would be paid, and that the debts and expenses, etc., designated to have priority would have priority of payment out of the estate after liens were satisfied, or out of the proceeds of the property if sold subject to liens. Since the striking out of the words 'sums to be paid as dividends and commissions,' in § 48, and the substitution of the words 'on all moneys disbursed by them,' and similar change in § 40 by the amendment of 1902, these commissions when necessary to be paid from funds subject to the liens, and which payment causes an abatement of the lien to that extent, gain the priority over liens by virtue of the reading of §§ 40 and 48 as amended, which sections now limit or modify subdivision b of § 64, and not by virtue of the reading of § 64. No corresponding amendment was made in § 64 of the Act as it was not regarded necessary. The directions of §§ 40 and 48 are plain and explicit, and must be read in connection with § 64. Only in exceptional cases does the necessity for applying the modification arise. I think it also clear that, should a case arise where a laborer has acquired a lien by virtue of the State lien law for wages earned within the three months before the commencement of proceedings, even should such lien largely exceed \$300, he would hold his lien and be entitled to full payment thereof notwithstanding clause 4 of subdivision b of § 64."

In *re Yoke Vitriified Brick Co.*, 25 A. B. R. 18, 180 Fed. 235 (D. C. Kans.): "In my judgment clauses 4 and 5 of § 64b of the Bankruptcy Act relate exclusively and alone to the subject of the right to priority of payment arising among those whose claims would, in absence of such clauses stand on terms of equality before the law as general unsecured claims, and that said clauses have no reference whatever to the subject of liens. * * * It was in contemplation of the law-making power that estates passing, as of the date of the adjudication, to the trustees in bankruptcy, would be covered and affected by fixed and valid liens resting thereon. Hence, for the protection of those holding such valid liens, and lest the rights of such lienholders should become confounded with the rights of those holding general unsecured demands against the estate which had been accorded priority in payment by the provisions of section 64b of the Act, it was provided in section 67d of the Act, in effect, that nothing appearing elsewhere in the act itself, no matter how general and comprehensive the language employed might be, should affect the validity, extent, or operation of such liens."

Also, priority is to be distinguished from expenses of administration. Thus, the rent for the receiver's or trustee's use and occupation of the premises, is not a "priority" but an "expense" of administration.³⁰

§ 2189. Federal and State Government and Municipality, as Priority Claimants.—The federal and state governments, municipal corporations, counties and quasi public corporations, in general, may be entitled to priority under § 64 (b) (5).³¹

³⁰. In *re Hersey*, 22 A. B. R. 860, 171 Fed. 1001 (D. C. Iowa).

³¹. In *re Western Implement Co.*, 22 A. B. R. 167, 166 Fed. 576 (D. C. Minn.,

affirmed sub nom. In *re Mercer*, 22 A. B. R. 413, 171 Fed. 81); In *re Mercer*, 22 A. B. R. 413, 171 Fed. 81 (C. C. A. Minn.).

Thus, the federal government may be a priority claimant, it has been held, under § 64 (b) (5); for instance, for damages for breach of contract by contractors;³² and it is not entitled to an earlier priority, ahead of workmen, clerks, traveling or city salesmen and servants, under United States Rev. Stats., § 3466.³³

Likewise, a county may be a priority claimant.³⁴

Likewise, a State government may be entitled to priority, it has been held, under § 64 (b) (5); for instance, for goods manufactured at the penitentiary and sold to a bankrupt.³⁵

§ 2190. Priority Given to "Any Person" by United States Law Preserved.—Priorities given to any person, by any of the laws of the United States, are preserved in bankruptcy.

Taxes do not come within § 64 (b) (5), but it is not necessarily because the government and State are not to be considered as being "any person" within the meaning of clause "5,"³⁶ nor is it because taxes are not to be considered "provable debts," as seems to be implied from the holding in *Chattanooga v. Hill*;³⁷ but it is rather because paragraph "(a)" of the same section of the statute specially provides the priority for taxes and therefore takes precedence over the general provisions of clause "5" of paragraph "(b)."

§ 2191. Government Contracts.—Damages suffered by the United States government are given, by federal statute,³⁸ priority of payment out of the funds in the hands of assignees, trustees in bankruptcy, executors, administrators, etc., in charge of insolvent estates. Thus, where a government contractor becomes bankrupt, the damages suffered by the government

32. In re Stoeber, 11 A. B. R. 345, 127 Fed. 394 (D. C. Pa.); Guaranty Co. v. Title Co., 224 U. S. 152, 27 A. B. R. 873, reversing on other point S. C., 23 A. B. R. 340, 174 Fed. 385 (C. C. A. Pa.), and aff'g 22 A. B. R. 851, — Fed. —.

33. See post, § 2191; also, see Guaranty Co. v. Title Co., 224 U. S. 152, 27 A. B. R. 873, reversing 23 A. B. R. 340, 174 Fed. 385 (C. C. A. Pa.).

34. In re Worcester Co., 4 A. B. R. 496, 102 Fed. 808 (C. C. A. Mass.). Compare, to same effect, under the law of 1867, In re Mellor, 10 Ben. 58, Fed. Cases No. 9,401; In re Southwestern Car Co., 9 Biss. 76, Fed. Cases No. 13,192; In re Dodge, 4 Dill. 532, Fed. Cases No. 3,949.

35. In re Western Implement Co., 22 A. B. R. 167, 166 Fed. 576 (D. C. Minn.), affirmed sub nom. In re Mercer, 22 A. B. R. 413, 171 Fed. 81 (C. C. A. Minn.).

36. In re Western Implement Co., 22 A. B. R. 167, 166 Fed. 576 (D. C. Minn.), affirmed sub nom. In re Mercer, 22 A. B. R. 413, 171 Fed. 81 (C. C. A. Minn.).

37. *Chattanooga v. Hill*, 15 A. B. R. 197, 139 Fed. 600 (C. C. A. Tenn.).

38. U. S. Rev. Stat., § 3466: "Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor in the hands of the executors or administrators is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority hereby established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts, makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed or absent debtor are attached by process of law, as to cases in which an act of bankruptcy is committed."

have priority of payment in bankruptcy,³⁹ and the surety paying the damages is subrogated to the same priority.⁴⁰

This priority of the government is governed by Bankr. Act, § 64 (b) (5), by which it is placed subsequent in order to the wages of workmen, clerks, salesmen and servants and it is not governed by United States Revised Statutes, § 3466.

Guaranty Title Co. v. Title Co., 224 U. S. 152, 27 A. B. R. 873, reversing S. C., 23 A. B. R. 340, 174 Fed. 385 (C. C. A. Pa.), which itself reversed 22 A. B. R. 851: "The Bankruptcy Act of 1867, as we have seen, provided for priority, first, for the payment of expenses, and, second, of 'all debts due to the United States, and all taxes and assessments under the laws thereof.'

"The priority, therefore, given by the Bankruptcy Act was co-extensive with the priority given by the statute of 1797. But there is not such affirmation by the Bankruptcy Act of 1898 of that statute, which still exists, as we have said, as section 3466 of the Revised Statutes, *supra*. There is a change in provisions, and we come to the question if there is a change of purpose. * * *

"It will be seen, therefore, that by the statute of 1797 (now section 3466) and section 5101 of the Revised Statutes, all debts due to the United States were expressly given priority to the wages due any operative, clerk, or house servant. A different order is prescribed by the Act of 1898, and something more. Labor claims are given priority, and it is provided that debts having priority shall be paid in full. The only exception is 'taxes legally due and owing by the bankrupt to the United States, State, county, district or municipality.'

"These were civil obligations, not personal conventions, and preference was given to them; but as to debts, we must assume a change of order. And we cannot say that it was inadvertent. The act takes into consideration, we think, the whole range of indebtedness of the bankrupt—national, State, and individual—and assigns the order of payment. The policy which dictated it was beneficent and well might induce a postponement of the claims, even of the sovereign, in favor of those who necessarily depended upon their daily labor. And to give such claims priority could in no case seriously affect the sovereign. To deny them priority would in all cases seriously affect the claimants."

39. *In re Stoeber*, 11 A. B. R. 345, 127 Fed. 394 (D. C. Penn.); *Guaranty Co. v. Title Co.*, 224 U. S. 152, 27 A. B. R. 873, reversing on other points S. C., 23 A. B. R. 340, 174 Fed. 385 (C. C. A. Pa.).

40. U. S. Rev. Stat., § 3468: "Whenever the principal in any bond given to the United States is insolvent, or whenever such principal, being deceased, his estate and effects which came to the hands of his executor, administrator or assigns, are insufficient for the payment of his debts, and in either of such cases any surety on the bond, or the executor, administrator or assigns of such surety pays to the United States the money due on such bond, such surety, his executor, administrator or assignees shall have the like priority for the recovery and receipt of the moneys out

of the estate and effects of such insolvent or deceased principal as is secured to the United States; and may bring and maintain a suit upon the bond in law or in equity, in his own name, for the recovery of all moneys paid thereon." See also, *Guaranty Co. v. Guarantee Co.*, 23 A. B. R. 340, 174 Fed. 385 (C. C. A. Pa.), quoted at § 2191.

But compare doubtful ruling in *United Surety Co. v. Iowa Mfg. Co.*, 24 A. B. R. 726, 179 Fed. 55 (C. C. A. Mo.), where the court held to be a preference the levy upon assets of a government contractor by a surety on the contract who had that same day advanced money to meet the current payroll, taking a judgment note therefor at the time.

§ 2192. No Proof of Claims Requisite by Government to Secure Priority.—Claims of the United States entitled to priority must be paid even without the filing of a proof of claim. It has even been held that the trustee takes his own risk in paying out the funds without taking care of such claims.⁴¹

§ 2193. Year's Limitation for Proving Claims Not Applicable to Government.—The limitation of one year for the proving of claims in bankruptcy does not apply to claims of the United States government.⁴²

§ 2194. State Law Priorities Adopted Where Claimants Not in Classes Already Covered by Express Bankruptcy Priorities.—Priorities given by state laws are adopted by § 64 (b) (5) of the Act, at any rate where the claimants are not in any of the classes already covered by express bankruptcy priorities. Thus, the claim of a county for the labor of its convicts is entitled to priority.⁴³

Thus, the priorities given by a State statute, granting priority to the claims of resident creditors over the claims of foreign corporations which have not complied with the State law regulating the doing of business by foreign corporations, have been recognized in bankruptcy.⁴⁴

However, as noted ante, § 2179, and post, § 2203, where the State priority covers the same class of claimants covered by § 64 (b) (4) of the Bankruptcy Act, the better rule is that the bankruptcy priority displaces the State priority.⁴⁵

§ 2195. State Priorities to Laborers, Where Different from Bankruptcy Priorities.—In some states other claimants than simply "workmen," "clerks," "salesmen" and "servants," as the latter terms are used in bankruptcy, are entitled to priority of payment out of the funds of an insolvent in the hands of a court, and the amount allowed and time of service for which priority is given also differ.⁴⁶

⁴¹. In re Stoeve, 11 A. B. R. 345, 127 Fed. 394 (D. C. Penn.). Compare, ante, § 2161.

⁴². In re Stoeve, 11 A. B. R. 345, 127 Fed. 394 (D. C. Pa.). Compare, ante, § 2162.

⁴³. In re Worcester Co., 4 A. B. R. 496, 102 Fed. 808 (C. C. A. Mass.); In re Wright, 2 A. B. R. 596, 95 Fed. 807 (D. C. Mass., affirmed sub nom. In re Worcester Co., 4 A. B. R. 496, 102 Fed. 808, C. C. A. Mass.).

Private Banker Doing Business in Several States, Depositors in One State Not Entitled to Share in Fund Deposited with Secretary of Another State.—It was held in one case that where a private banker did business in several different states, in New Jersey, Pennsylvania, Ohio and New York, the depositors of the other States could

not share in a fund of \$100,000 deposited in accordance with law with the Comptroller of the State of New York. In re Rosset, 29 A. B. R. 341, 203 Fed. 67, D. C. New York.

⁴⁴. In re Standard Oak Veneer Co., 22 A. B. R. 883, 173 Fed. 103 (D. C. Tenn.), quoted at § 2196.

⁴⁵. In re Rouse, Hazard & Co., 1 A. B. R. 234, 91 Fed. 96 (C. C. A. Ills.); In re Slomka, 9 A. B. R. 635, 122 Fed. 630 (C. C. A. N. Y.), quoted ante, § 2179; contra, In re Laird, 6 A. B. R. 1, 109 Fed. 550 (C. C. A. Ohio), discussed by same court in In re Bennett, 18 A. B. R. 320, 153 Fed. 673.

⁴⁶. Instance, for furnishing materials and supplies to manufacturing concern, In re Falls City Shirt Mfg. Co., 3 A. B. R. 437, 98 Fed. 592 (D. C. Ky.).

In re Lawler, 6 A. B. R. 184, 110 Fed.

Compare, stronger statement of rule, *In re Rose*, 1 A. B. R. 68 (Ref. Ohio): "The provisions of (5) make it the duty of the court to consider, not only § 64 of the Bankruptcy Act, but the sections of the statutes of the State, and it would be the duty of the court to grant the demands of the claimants if it should find that their respective claims fall within the protection of any of the laws of either."

§ 2196. Whether State Priorities in Cases of Assignments, Receiverships, etc., Preserved When Custody Superseded by Bankruptcy.—Priorities given by the state statutes seem to have been recognized in the bankruptcy court even where such priorities arise by virtue of assignments for the benefit of creditors, receiverships, or other sequestrations by legal proceedings eventually nullified or supplanted by bankruptcy proceedings. The state court is superseded, to be sure, but apparently it is held, by these decisions, that the general priorities recognized by its policy in the distribution of insolvent estates are to be recognized as additional priorities in bankruptcy under § 64 (b) (5).⁴⁷

In re Jones, 18 A. B. R. 212, 151 Fed. 108 (D. C. Mich.): "The principle controlling these decisions seems to be that a creditor shall be allowed the same priority under the Bankrupt Act which he would have had, had not the latter Act superseded the State laws governing the distribution of the estates of insolvent debtors. Tested by this rule the question is: Would the petitioners have been given the priority claim here, had the debtor's estate been distributed under the laws of Michigan governing the distribution of the estates of insolvents instead of under the Bankrupt Act."

Obiter, *In re Yoke Vitrified Brick Co.*, 25 A. B. R. 18, 180 Fed. 235 (D. C. Kans.): "The statute of the State on which petitioners rely, above quoted, is an insolvency law of this State. While its repeal was not affected by the passage of the Bankruptcy Act, yet its operation was suspended during the period the Bankruptcy Act shall remain in force. *Butler v. Goreley*, 146 U. S. 303, 13 Sup. Ct. 84, 36 L. Ed. 981. And were it not for the fact that clause 5 of section 64b of

135 (D. C. Wash.): In this case the court held that a person who was engaged as a traveling salesman for a lumber company was a "person performing labor" for such company, and entitled to priority under the statute of Washington, giving a prior lien to persons performing labor for any person, company or corporation in the operation of any sawmill, lumber or timber company.

Compare, *In re Byrne*, 3 A. B. R. 268, 97 Fed. 762 (D. C. Iowa).

⁴⁷ Compare, *ante*, § 1266. Also, see *In re Floyd & Behr Co.*, 29 A. B. R. 149, 200 Fed. 1016 (D. C. Ky.). Inferentially, *In re Lewis*, 4 A. B. R. 51, 99 Fed. 935 (D. C. Mass.); *obiter*, *In re Burton Bros. Mfg. Co.*, 14 A. B. R. 218, 134 Fed. 157 (D. C. Iowa); instance, but not placed on this ground, *In re Laird*, 6 A. B. R. 1 (C. C. A. Ohio): This case, however, violates the rule that the Bankruptcy Act con-

trols as to priorities as to the same classes covered by the state law.

Impliedly and a fortiori, *In re Iroquois Mach. Co.*, 22 A. B. R. 183, 166 Fed. 629 (D. C. R. I.); compare, *In re Bennett*, 18 A. B. R. 320, 153 Fed. 673 (C. C. A. Ky.), discussing *In re Laird*, *supra*. *In re Standard Oak Veneer Co.*, 22 A. B. R. 883, 173 Fed. 103 (D. C. Tenn.), quoted at § 2196. Impliedly, *In re Amoratis*, 24 A. B. R. 565, 178 Fed. 919 (C. C. A. Calif.), quoted at § 2197. But compare, analogously, *contra*, *In re Monroe Lumber Co.*, 24 A. B. R. 371 (D. C. Miss.), quoted and discussed at § 1155, note 37. *Contra*, *In re Slomka*, 9 A. B. R. 636, 122 Fed. 630 (C. C. A. N. Y.), where the rule is laid down that the priority being given only because of the assignments, and the assignment itself being nullified by the bankruptcy, the priorities fall along with the assignment—a logical argument at any rate.

the Bankruptcy Act preserves such statute in effect as a law of the State touching the subject of priorities, it would remain entirely inoperative and of no force in the settlement of estates of bankrupts under the provisions of the Bankruptcy Act."

Thus, where the costs of an attachment, which itself is dissolved by subsequent state insolvency or assignment proceedings, are nevertheless given priority by state law in such subsequent insolvency or assignment proceedings, they will be accorded the same priority in bankruptcy distribution.⁴⁸

Probably the question would turn in each case upon the point whether the statute in the particular instance is attempting to create *general* rights of priority in cases where insolvent estates are being administered, or simply to create certain rights of priority in case certain methods of distribution of insolvent estates are being pursued.

In re Jones, 18 A. B. R. 214, 151 Fed. 108 (D. C. Mich.): "Previous to the passage of the present Bankrupt Act, estates of insolvent debtors were usually, if not universally, administered in Michigan under either common-law assignments (later regulated by the general assignment statute of 1879), mortgage foreclosure, or receivership in some form. They have seldom, if ever, been administered under chapter 262, which relates to the 'Relief of Insolvent Debtors,' although the provisions of chapter 263, relating to the 'Relief of Insolvent Debtors from Imprisonment,' have been occasionally invoked, although rarely, as under the Michigan Constitution imprisonment, for debt generally is forbidden. Const. Mich. art. 6, § 53. The reports of the Supreme Court of Michigan fail to show that any case arising under chapter 262, or any case involving the application of § 9675 in question, have ever been brought before that court. As indicating what is meant by a general insolvency statute, it is significant that the labor preference statute referred to has been applied to the distribution of the estates of insolvents, not only under mortgage foreclosure by way of intervention * * *, under statutory assignments for the benefit of creditors, in which preferences are forbidden * * *, but also under original bill filed against mortgage and attaching creditors in possession of the debtors' assets. * * * This labor preference statute would probably be similarly extended to receiverships, as was done in Massachusetts; the Michigan statute making express provisions for granting receiverships for the protection of labor claimants. 3 Comp. Laws 1897, § 9552. It would also, no doubt, apply to bankrupt estates, but for the fact that the Bankrupt Act contains express provisions on the subject of preference for labor debts which override the provision of the statute law. * * *

"On the other hand, and in sharp contrast to the general application of the labor insolvency statute, to none of these methods of administration and distribution of the estates of insolvent debtors under the State law has any attempt ever been made to apply the provisions of § 9675, here invoked, and doubtless for the reason that that section is by its terms limited to proceedings under the chapters included within the title in the 1846 revision, 'Of the Punishment of Fraudulent debtors and the Relief of Insolvent debtors.' In the absence of a bankruptcy statute, had the estate of this bankrupt been administered as an insolvent estate under Michigan laws, under either assignment for benefit of creditors, mortgage foreclosure, or receivership, or by any method except that provided by chapter 262 and 263 of the Michigan Compilation, the priority

⁴⁸. A fortiori, In re Iroquois Mach. Co., 22 A. B. R. 183, 166 Fed. 629 (D. C. R. I.), quoted post, § 2197.

invoked would not have been recognized. The possibility of such estate being administered under chapters 262 or 263 would be very slight. As before stated, such administration could occur only by way of relief from actual imprisonment or, otherwise, only with concurrence of the debtor and creditors representing at least two-thirds of all debts owing to creditors within the United States. To my mind, § 9675 is, therefore, not 'of that general character which can be supposed to be within the purview of the provision of the Bankrupt Act which is concerned here,' and not such a 'law of the State' as to give priority under § 64b (5) of the Bankrupt Act. It follows that the referee rightly refused priority to petitioners' claims."

Thus, it has been held that the bankruptcy court will recognize in the distribution of the assets of a bankrupt foreign corporation the priority of the claims of resident creditors over the claims of foreign corporations which have not complied with the statute regulating the doing of business within the state by foreign corporations, such statute (whether constitutional or not being beside the question here involved) conferring substantive rights of priority rather than rights dependent upon resort to particular state remedies.

In re Standard Oak Veneer Co., 22 A. B. R. 883, 173 Fed. 103 (D. C. Tenn.): "It is also urged in behalf of petitioners that, although § 64b (5) of the Bankruptcy Act provides that in the administration of the bankrupt's estate priority shall be given to 'debts owing to any person who by the laws of the State or the United States is entitled to priority,' the provision of the Act of 1877 should be regarded as an insolvency law in reference to foreign corporations, which was superseded by the Federal Bankruptcy Act, and that hence the priorities which it gives should not be recognized. While, however, it is true that the enactment of the Federal Bankruptcy Act superseded all State insolvency or bankruptcy laws relative to persons or acts declared by the Congress to be subjects of bankruptcy, so that no further proceedings could be had under such State laws (1 Remington on Bankruptcy, p. 993, § 1628), yet this rule relates merely to the administration of the State laws in proceedings in the State courts, and does not prevent the enforcement in the Federal bankruptcy proceedings of any general priorities recognized by the State laws, where such priorities are conferred by the State statutes as substantive rights of priority not dependent upon the resort to particular remedies accessible only in proceedings in the State courts, and where such priorities are not in conflict with the express priorities declared by the Federal Bankruptcy Act itself or otherwise in conflict with its provisions. 2 Remington on Bankruptcy, p. 1346, et seq., §§ 2194, 2198. Furthermore, the rule relied on by petitioners can have no application to the statutes in question, which are not, strictly speaking, State insolvency laws within the general rule of suspension, but merely statutes prescribing the conditions upon which foreign corporations may enter the State for purposes of business."

§ 2197. Whether State Priorities Dependent on Resort to Particular Remedies, Such as Insolvency or State Bankruptcy Proceedings, to Be Recognized.—Whether or not priorities will be recognized in the distribution of an estate in bankruptcy that are given by a state statute in the event that assets are sequestrated by state insolvency or state bankruptcy proceedings, or by assignments, receiverships or other

state proceedings involving the administration of an insolvent's assets, as an additional priority under § 64 (b) (5), when such state proceedings have not actually been instituted, is also to be determined by the ascertainment of the true intent of the state statute. If the state statute means to confer the priorities as substantive rights of priority in cases of the distribution of insolvent estates in general, then of course the priority is to be recognized in bankruptcy distribution; but if, on the contrary, the right is wholly special and dependent upon resort to a particular remedy, then, obviously, if that remedy is inaccessible, the priorities must likewise fail of recognition in bankruptcy.⁴⁹ Even the priorities of suspended insolvency statutes are adopted where not covering the same cases covered by the express provisions of the Bankrupt Act and where the priorities are intended to be given as substantive rights, not dependent on resort to a particular remedy.⁵⁰

Some of the decisions, however, have carried the adoption of State priorities to an unwarranted extreme; in effect, nullifying thereby the provisions of the Bankruptcy Act dissolving legal liens, and leaving to creditors no advantage in dissolving liens, their priorities being nevertheless perpetuated!!

Thus, it has been held, that where attachment costs could have had priority had State insolvency or assignment proceedings actually been instituted, they will have priority in bankruptcy, under § 64 (b), (5), even though such proceedings have not been instituted.⁵¹

In *re Goldberg*, 16 A. B. R. 523, 144 Fed. 566 (D. C. Me.): “* * * the clear intention of the Maine statute is that such costs shall be paid out of the estate, if it appears to the court that the suit was commenced in good faith for the benefit of all the creditors. The intention of the Maine legislature was to pay such costs in full out of the estate, providing the estate had received an actual benefit by incurring such costs, just as it is the intention of Congress to pay the actual and necessary cost of preserving the estate subsequent to filing a petition in bankruptcy. Courts in other circuits have disallowed such claims; but these disallowances have been based generally; so far as I can find, upon the fact that the statutes of the States where the questions arose did not provide for their allowance in terms so specific as the statutes of Massachusetts provided.”

In *re Iroquois Mach. Co.*, 22 A. B. R. 183, 166 Fed. 629 (D. C. R. I.): “It seems to be very clear that it has been for many years the clearly defined policy of the State of Rhode Island, as expressed in its former and present general insolvency laws, as well as in the act regulating general assignments, that, whenever for the benefit of the general creditors an attachment is dissolved, the costs justly accruing prior to the moment of dissolution should be regarded as a charge upon the funds. * * * It is true that in the present case there

49. In *re Jones*, 18 A. B. R. 214 (D. C. Mich.). Impliedly, In *re Standard Oak Veener Co.*, 22 A. B. R. 883, 173 Fed. 103 (D. C. Tenn.), quoted ante, § 2196. See ante, § 1266.

But compare (as to laborers' liens, not their priorities), In *re Monroe Lumber Co.*, 24 A. B. R. 371 (D. C. Miss.), quoted at § 1155, note. It is difficult to gather from this decision whether the laborers' rights were con-

sidered to be in the nature of liens—in which event the principles of §§ 1437, 1444, 1586, would apply—or in the nature of priorities. The wording of the state statute would seem to classify them as liens.

50. In *re Yoke Vitrified Brick Co.*, 25 A. B. R. 18, 180 Fed. 235 (D. C. Kan.).

51. In *re Lewis*, 4 A. B. R. 51, 99 Fed. 935 (D. C. Mass.).

had been no assignment for the benefit of creditors, but the recognition by the United States court of priorities under the laws of the State is not dependent upon acts of the parties under State laws, but rather upon the existence of statutes clearly defining the policy of the State under circumstances similar to those arising under the bankruptcy administration. * * * It seems to be the policy of the Bankruptcy Act to recognize both exemptions and priorities created by the State law, though this leads to some diversity in the administration of the Bankruptcy Act in various administrations."

Even though the attachment were prompted by the desire to get a preference the priority of its costs under State law might not be impaired.

In *re Amoratis*, 24 A. B. R. 565, 178 Fed. 919 (C. C. A. Calif.): "In like circumstances they would have been provable and entitled to priority in insolvency proceedings under the California statute cited. The fact that under that statute a claim for such costs is entitled to priority, even though the proceedings by the attaching creditor were prompted by the desire to secure a preference, does not, in our opinion, deprive the attaching creditor, whose good faith brings him within the provisions of the Bankruptcy Act, as well as of the State Insolvency Act, of priority for such costs necessarily expended."

But there would be difficulty in determining which order of priority should thus be adopted by analogy, where the state law prescribes different priorities for different methods of sequestration.⁵³

Compare, In *re Rouse, Hazard & Co.*, 1 A. B. R. 239, 91 Fed. 96 (C. C. A. Ills.): "Coming then to the merits, it may be remarked by the way of preface that the several provisions of the law of the State of Illinois with respect to the priority of payment to be allowed labor claims, are not altogether consistent. In the case of voluntary assignments, the claim of the laborer which is preferred must have accrued within three months next preceding the making of the assignment. In the case of a suspension of business by action of creditors there is neither limit as to time nor as to amount. The reason of the distinction is not easy to understand."

The claim of the state or county for the hire of its convicts, has been given priority in bankruptcy, though such priority would not exist under the state statute except in cases of state insolvency or state bankruptcy proceedings, which had not in fact been instituted and which indeed were not maintainable because of the existence of the Federal Bankrupt Act.⁵⁴

In *re Wright*, 2 A. B. R. 594, 95 Fed. 807 (D. C. Mass., affirmed sub nom. In *re Worcester Co.*, 4 A. B. R. 496, 102 Fed. 808, C. C. A. Mass.): "Even if by the passage of the Bankrupt Act the insolvent law of Massachusetts were so avoided that it has ceased to be a law of Massachusetts, yet nothing would prevent the legislature of Massachusetts, during the existence of the Bankrupt Law, from passing a statute establishing priorities. Such a statute would have almost its sole effect in establishing priorities under the Bankrupt Law of the

53. In Maryland priority in bankruptcy distribution is refused to landlords who have not levied distress before bankruptcy, following the rule in cases of assignments and insolvencies under the State law, even though by

chancery practice in the winding up of corporations a different rule seems to prevail. In *re Chaudron & Peyton*, 24 A. B. R. 811, 180 Fed. 841 (D. C. Md.).

54. In *re Worcester Co.*, 4 A. B. R. 496, 102 Fed. 808 (C. C. A. Mass.).

United States. It would be simply a re-enactment of the rule regarding the distribution of insolvent estates which had prevailed by statute up to the passage of the Bankrupt Law. To suppose that Congress meant to require such legislation by the States is unreasonable."

Thus, it has been held that even costs of a suit might be entitled to priority in bankruptcy, if entitled to priority under the state insolvency laws.⁵⁵

Obiter, In re Daniels, 6 A. B. R. 700, 110 Fed. 745 (D. C. R. I.): "It must, therefore, be accepted as the law of this circuit that, in determining what laws of a State are in force for the purpose of fixing priorities, we may look to the insolvency laws * * * the insolvency law of a State still remains a law for the purpose of fixing priorities. * * *

"The decision of the referee, then, cannot be supported upon the broad ground that in no case can the costs which are preferred under the insolvency law of Rhode Island be entitled to priority, under § 64b (5) of the Bankruptcy Act."

Although, of course, any *lien* therefor, if acquired within the four months, would be avoided by § 67 "f."⁵⁶

§ 2198. Rule Adopting State Priorities, Not to Override § 67 "f" Annuling "Legal" Liens.—But the rule adopting state priorities is not meant to override the provisions of § 67 "f" annulling liens by legal proceedings obtained within four months of the debtor's bankruptcy. Section 64 (b) (5) is not concerned with *liens* acquired by legal proceedings, but with *priorities on distribution of an insolvent's assets*.

In re Burton Bros. Mfg. Co., 14 A. B. R. 218, 134 Fed. 157 (D. C. Iowa): "These sections, as construed by the Supreme Court of Iowa, when complied with, give priority of payment to the wage-earning employee, to the amount stated, from the property of the employer which has been so seized upon execution, or placed in the hands of a receiver, trustee, or assignee over all other liens upon such property (except certain mechanics' liens) and other creditors of the employer. * * * Neither of the petitioners ever presented to the officer making such seizure, or to the court from which the execution issued, the sworn statement required by section 4020 of the Code, nor in any other manner complied with the provisions of the above named sections. They apparently relied solely upon the levy of their executions upon the property to secure payment of their judgments, and nothing further seems to have been done after such levy and prior to August 20, 1904, when the petition in bankruptcy was filed against the judgment debtors. The adjudication of bankruptcy upon that petition dissolved the liens of the petitioners acquired by the levy of their executions upon the property of the bankrupt. * * *

"To have secured and preserved the right or liens given them by the State statute the petitioners should have complied with the provisions of that statute, and had they done so such right or lien might have been recognized and enforced by the court of bankruptcy. Section 64b (5), Bankruptcy Act. Not having done so, the only lien they had was that acquired by the seizure of the

⁵⁵. In re Goldberg, 16 A. B. R. 523, 144 Fed. 566 (D. C. Me.), quoted supra; In re Amoris, 24 A. B. R. 565, 178 Fed. 919 (C. C. A. Calif.), quoted supra. But compare, next section, § 2198.

⁵⁶. In re The Copper King, Limited, 16 A. B. R. 148, 143 Fed. 649 (D. C. Calif.).

property under their executions. When such liens were dissolved by the adjudication of bankruptcy, they were left upon a level with the other unsecured creditors of the bankrupt."

The priority is not given *because* of the legal proceedings being superseded, but because it is usually in connection with those legal proceedings which are nullified by bankruptcy that the state statute mentions its priorities.

And, in cases where the priority is held only to exist in case a particular method of administering the insolvent's estate is adopted, then the priority may not be adopted in bankruptcy, where the requisite administration cannot be had because of § 67 "f."

Compare, *In re Slomka*, 9 A. B. R. 636, 122 Fed. 630 (C. C. A. N. Y.): "The State statute does not purport to give employees a lien upon the property of the employer for wages, nor to give them priority over other creditors of the debtor except when the debtor's estate is distributed by an assignee under a general assignment. In that event it impresses the funds in the hands of the assignee with a trust. *Richardson v. Thurber*, 104 N. Y. 606. If the estate is not distributed under the assignment, as for instance if the assignment should be set aside for fraud or for invalidity otherwise, the provision is nugatory. There was no priority here, because the conditions essential to its recognition did not exist. The assets were not in course of administration under a general assignment. * * * The assignment being void, it is as though it had never been made, and the property of the debtor passed to the trustee in bankruptcy free from all liens or trusts created by or resulting from it."

And as to costs, likewise, the better opinion is that wherever the lien of the attachment or other process would be dissolved by § 67 "f" then the priority of the costs likewise would not exist, and that the effect of § 67 "f" could not be evaded as to the costs by claiming they are entitled to priority under § 64 (b) (5).⁵⁷

Yet, the Circuit Court of Appeals construing the same insolvency statute has held that the priority does exist for the costs.⁵⁸

In re The Copper King, 16 A. B. R. 148, 143 Fed. 649 (D. C. Calif.): "In some of the States certain classes of debts arising upon contract are entitled to priority of payment in the distribution of estates. * * * It was the purpose of subdivision 5, § 64, of the Bankruptcy Act, to preserve the rights of creditors under such contracts; and it may extend to an indebtedness upon an implied contract which is given priority by a law of the State. But, in view of the fact that attachment liens obtained within four months prior to the filing of the petition, including the lien for costs in the attachment proceedings, are dissolved by subdivision 'c' and 'f' of § 67, of the Bankruptcy Act, it is not reasonable to conclude that Congress intended by subdivision 5, of § 64, to make the claim for costs, the lien of which is thus destroyed, a preferred debt."

⁵⁷ *In re The Copper King Ltd.*, 16 A. B. R. 148, 143 Fed. 649 (D. C. Calif.). Contra, impliedly, *In re Amoratis*, 24 A. B. R. 565, 178 Fed. 919 (C. C. A. Calif.), quoted *supra*.

⁵⁸ *In re Amoratis*, 24 A. B. R. 565, 178 Fed. 919 (C. C. A. Calif.), quoted at § 2197.

And perhaps the true principle is that the bankruptcy courts have nothing at all to do with superseded or suspended state insolvency acts in determining priorities in the distribution of bankrupt estates.

Smith v. Mottley, 17 A. B. R. 865, 150 Fed. 266 (C. C. A. Ohio): “* * * he referred to its insolvency laws, which specify what liabilities shall be preferred in insolvency proceedings. * * * But we think there was error in holding that the Kentucky Insolvency Statute was relevant to the inquiry. That statute was superseded by the Bankruptcy Act, which itself prescribes what debts and obligations shall be given preference.”

§ 2199. But Claimant Must Comply with All Regulations and Prerequisites of State Priority.—But the claimant must comply with all the statutory prerequisites and conditions required by the state law where he is making his claim in the bankruptcy court. Thus, where an employee forfeits his priority if he fails to comply with the provisions of the state law requiring a sworn statement of the employee's claim to be presented to the officer making the seizure or to the court from which the execution issued, he forfeits it in the bankruptcy court under the same circumstances.⁵⁹ And where a priority given by a state statute is to be perfected in a particular manner (not rendered impossible by the bankruptcy), such manner must be pursued.⁶⁰

Grainger & Co. v. Riley, 29 A. B. R. 114, 201 Fed. 901 (C. C. A. Ky.): “The statute authorizes a lien in favor of mechanics, laborers and materialmen, and provides that no person shall acquire this lien, unless he shall notify in writing the owner of the property to be held liable or his authorized agent, immediately after the last item of material or labor is furnished, of his intention to hold the property liable, and the amount for which he claims a lien. Nothing is left to inference or conjecture. A compliance with this provision is, as we think, *conditio sine qua non*.”

§ 2200. Whether, Where Bankruptcy Prevents, Compliance Dispensed with, or Levy Permitted and Discharge Stayed to Enable Perfecting of Priority.—Where a priority or lien given by a State statute is declared to be lost unless followed by legal proceedings within a specified time, either such condition subsequent is avoided by the bankruptcy, since the property involved is already in the custody of a court and further legal proceedings are impossible,⁶¹ as, for instance, where a landlord is prevented from perfecting his lien by distraint.

^{59.} In *re* *Burton Bros. Mfg. Co.*, 14 A. B. R. 218, 134 Fed. 157 (D. C. Iowa).

^{60.} In *re* *Burton Bros. Mfg. Co.*, 14 A. B. R. 218, 134 Fed. 157 (D. C. Iowa).

Compare, In *re* *Bennett*, 18 A. B. R. 320, 153 Fed. 673 (C. C. A. Ky.), wherein it was held that the particular priority therein concerned—for furnishing materials for a manufacturing concern—did not require recording.

Compare similar rule in regard to exemptions, § 1048.

Compare, inferentially, In *re* *Monroe Lumber Co.*, 24 A. B. R. 371 (D. C. Miss.), quoted and discussed at § 1155, note 57.

^{61.} In *re* *Falls City Shirt Mfg. Co.*, 3 A. B. R. 437, 98 Fed. 592 (D. C. Ky.). But compare, In *re* *Monroe Lumber Co.*, 24 A. B. R. 371 (D. C. Miss.), quoted at § 1155, note.

In *re Bishop*, 18 A. B. R. 635, 153 Fed. 304 (D. C. S. Car.): "The court, however, holds that inasmuch as by this action in taking possession of the property the landlord is prevented from making an actual levy and distress, that the court will permit him to present his claim as a preferred claim, and claim in priority what is due to him as landlord."

Or perhaps the bankruptcy court would permit the legal proceedings to be taken, at least to the extent necessary to perfect or maintain the lien.⁶²

§ 2201. Whether Trustee Can Perfect Priority Claims.—The trustee cannot perfect the claims of the priority creditors where the State statutes require further proceedings. He does not represent secured or priority creditors except as mere custodian;⁶³ although his seizure may incidentally affect their rights.

§ 2202. Relative Precedence among State Priorities Preserved.—The relative priorities among the different classes of claimants entitled to priorities under the state law will be preserved; and § 64 (b) (5) of the Bankruptcy Act does not level them to equality among themselves.⁶⁴

Thus, the relative priorities of the landlord over persons who have furnished material or supplies for a manufacturing concern, under the Kentucky statute, are preserved in bankruptcy.⁶⁵

In *re Falls City Shirt Mfg. Co.*, 3 A. B. R. 437, 98 Fed. 592 (D. C. Ky.): "The effect of the contention of the material men here would be that though all the creditors had liens created under the laws of the State, and though by those laws some of these liens had priority over others, still a proper interpretation of the Bankrupt Act would require a general leveling of these liens to a common plane, elevating some and depressing others, so as to destroy all advantage and all distinction given by the State laws. It cannot be admitted that such contention is sound. It seems to the court that it was obviously the intention of Congress to recognize all liens created under the laws of the State, and to leave them precisely as it found them."

And, in Arkansas, Georgia and Iowa, and in several other States labor claims take precedence over valid prior contract liens or landlord's statutory liens, and are entitled to like precedence in bankruptcy.⁶⁶

⁶². Compare, analogously, as to the necessity of judgment against corporation to fix stockholder's secondary liability, in some states, *In re Marshall Paper Co.*, 4 A. B. R. 468, 102 Fed. 872 (C. C. A. Mass.). Also, see ante, "Staying Discharge and Permitting Creditor to Take Judgment to Fix Liability on Surety," § 1524.

⁶³. Analogously, *Goldman v. Smith*, 2 A. B. R. 104 (Ref. Ky.).

⁶⁴. In *re Riehl*, 29 A. B. R. 613, 200 Fed. 455 (D. C. Md.); Compare, inferentially, *In re Yoke Vitrified Brick Co.*, 25 A. B. R. 18, 180 Fed. 235 (D. C. Kans.).

⁶⁵. But the trustee may not be surcharged by the landlord because of the

fact that by running the bankrupt's hotel he has permitted liens for supplies to acquire precedence over the landlord's priority for rent, the landlord having taken no steps to cause the hotel to be shut, compare, ruling in Pennsylvania, *In re Bayley*, 22 A. B. R. 249 (D. C. Pa.).

Right of Distraint in Pennsylvania Not Superior to Execution Lien.—*In re DeLancey Stables Co.*, 22 A. B. R. 406, 170 Fed. 860 (D. C. Pa.).

⁶⁶. Instance, *Chauncey v. Dyke Bros.*, 9 A. B. R. 444, 119 Fed. 1 (C. C. A. Ark.); *In re Erie Lumber Co.*, 17 A. B. R. 698 (D. C. Ga.); *In re Oconee Mill Co.*, 6 A. B. R. 475, 109 Fed. 866 (C. C. A. Ga.).

Instance, *In re Byrne*, 3 A. B. R. 270, 97 Fed. 762 (D. C. Iowa): "It thus appears that, under the laws of this State, when an insolvent estate is being closed up through the medium of a receiver, trustee, or assignee, the wages due employees, up to the amount of \$100 to each person, for work done within ninety days next preceding the seizure by judicial process, or the transfer to the receiver, trustee or assignee of the property of the insolvent, will be given preference in order of payment over contract liens existing thereon; and the same preference must be given to wages due employees over liens created by statute, such as the landlord's claim on behalf of Runyan."

§ 2203. Where Both State Law and Bankrupt Act Give Priority to Same Class, Bankrupt Act Excludes State Law.—Where both a State law and the Bankruptcy Act give priority to the same class of debts, the Bankrupt Act not only controls the State law in the case of absolute conflict between the two, but by its express regulation of these priorities, excludes the state law altogether.⁶⁷

In *re Crown Point Brush Co.*, 29 A. B. R. 647, 200 Fed. 882 (D. C. N. Y.): "Hence, the fact that in dealing with workmen, clerks, traveling or city salesmen and servants the State law may be broader and more liberal than the Bankruptcy Act is no warrant for enlarging the priority given those classes by the Bankruptcy Act. The claimants here allege they belong to one of the classes—workmen, clerks, or servants. The Bankruptcy Act gives priority to each of those classes; and hence the Bankruptcy Act itself controls the decision of this case, whatever the State court may have held as to the breadth and scope of the statutes of the State giving priority to the same classes."

Thus, where the priority claimants under the state statute would also fall within the class of "Workmen, clerks, salesmen or servants" as the terms are used in the Bankruptcy Act, the provisions of the Bankruptcy Act will prevail over those of the State statute, the specific words of the Bankruptcy Act taking out of its general words the subjects specified and confining them within the limits mentioned.⁶⁸

In *re Rouse, Hazard & Co.*, 1 A. B. R. 234, 91 Fed. 96 (C. C. A. Ills.): "In the first subdivision Congress addresses itself to the subject of labor claims, and particularly provides that all wages that have been earned within three months before the date of the commencement of proceedings in bankruptcy, not to exceed \$300 to each claimant, shall be awarded priority of payment. If recognized, it must be assumed, the various provisions of law in the several States with respect to the subject. It found them not to be in harmony, and in

⁶⁷. In *re McDavid Lumber Co.*, 27 A. B. R. 39, 190 Fed. 97 (D. C. Fla.); compare, on the facts where state law gave six months instead of three months, *In re Yoke Vitrified Brick Co.*, 25 A. B. R. 18, 180 Fed. 235 (D. C. Kans.); obiter, *In re Cress-McCormick Co.*, 25 A. B. R. 464 (Ref. Miss.).

⁶⁸. But compare, *In re Gerson*, 1 A. B. R. 251 (Ref. Penn.). Compare, to same general effect, *Smith v. Motley*, 17 A. B. R. 865 (C. C. A. Ohio); analo-

gously, *In re Daniels*, 6 A. B. R. 699, 110 Fed. 745 (D. C. R. I.); contra, *In re Laird* (*In re Coe-Powers & Co.*), 6 A. B. R. 1, 109 Fed. 550 (C. C. A. Ohio), disapproved in *In re Slomka*, 9 A. B. R. 635, 122 Fed. 630 (C. C. A. N. Y.), and apparently receded from in *Smith v. Motley*, 17 A. B. R. 865 (C. C. A. Ohio), but explained and reaffirmed in *In re Bennett*, 18 A. B. R. 320, 153 Fed. 673 (C. C. A. Ohio).

some States, as notably Illinois, the laws upon that subject not to be consistent with each other. It found limitation as to time different in the different States. It found that in some of the States priority of payment was unlimited as to amount, and in some of the States limited to so small a sum as \$50. With this divergence within its knowledge, the Congress spoke to the subject specially and particularly, and limited the amount to \$300, and, as to time, to wages earned within three months before the commencement of proceedings. Can, then, the subsequent provision of the law following immediately thereafter allowing priority of payment for all debts owing to any person who by the laws of the State or the United States, is entitled to priority, be held to enlarge the prior provisions so that the statute should be read that in any event the laborer should be entitled to priority of payment in respect of wages earned within three months prior to proceedings and in amount not exceeding \$300, and that wherever the laws of the State of the residence of the bankrupt grant the laborer priority of payment without limit as to time or amount, or imposes a limit in excess of that imposed by the Bankrupt Act, he shall be entitled to a further priority in payment according to the law of the particular State. We think not. It is not to be supposed—unless the language of the act clearly so speaks—that Congress intended that in the administration of the act there should be a marked contrariety in the priority of payment of labor claims dependent upon locality. It is an elementary principle of construction that where there are in one act, or in several acts contemporaneously passed, specific provisions relating to a particular subject, they will govern in respect to that subject as against general provisions contained in the same act. *Sutherland on Statutory Construction*, § 158."

In *re Slomka*, 9 A. B. R. 635, 122 Fed. 630 (C. C. A. N. Y.): "If by the State law the debts were within the general description of clause 5, we are of opinion that the clause would not apply and that the terms of clause 4 supply the exclusive rule for determining what debts for wages are entitled to priority. No principle of statutory construction is better settled than that which displaces the application of general provisions to a particular subject when there are specific provisions applicable to it in the same act. The subject of claims for wages is specifically regulated by clause 4, and its provisions express the particular intent of Congress regarding priority of such claims. As these confine the priority to wages earned within the three months before the commencement of the bankruptcy proceedings, debts like the present are not included. We agree upon this question with the decision of the Circuit Court of Appeals for the Seventh Circuit, *In re Rouse, Hazard & Co.*, 1 Am. B. R. 234, 91 Fed. Rep. 96, and for the reasons which are so satisfactorily stated in the opinion in that case. We have given due consideration to the decision by the Circuit Court of Appeals for the Sixth Circuit, *In re Laird*, 6 Am. B. R. 1, 109 Fed. 550, but we are unable to regard it as correct."

In *re Shaw*, 6 A. B. R. 501, 109 Fed. 782 (D. C. Penn.): "I agree with the correctness of this ruling (*In re Rouse, Hazard & Co.*) which, indeed, seems to me to be scarcely susceptible of doubt. Paragraph 4 deals specifically with the allowance of claims for wages; and, while it is true that wages might be included under the general word 'debts,' used in paragraph 5, thus to include them would violate a well known rule of statutory construction. Having been specifically dealt with in the paragraph immediately preceding, it is almost incredible that Congress should straightway proceed to deal with them again in a different fashion. To declare that they are included under the words 'debts' would be either to strike paragraph 4 out of the act entirely, or to furnish two conflicting rules for deciding how much should be allowed to a claim for wages

in priority. The result, of course, would be that a claimant could select whichever paragraph gave him the larger sum. I need scarcely say that such a result does not furnish a rule of decision, and could only be accepted in case the language used by Congress forbade any other construction. The ordinary and natural construction is, I think, that paragraph 4 has to do with wages, and paragraph 5 has to do with other debts entitled to priority."

Impliedly, *In re Wright*, 2 A. B. R. 592, 600, 95 Fed. 807 (D. C. Mass., affirmed sub nom. *In re Worcester Co.*, 4 A. B. R. 496, 102 Fed. 808): "In *re Rouse, Hazard & Co.*, 33 C. C. A. 356, 91 Fed. 96 (1 Am. B. R. 234), it was held that a claim for labor performed more than three months before the bankruptcy proceedings, and entitled to priority under the insolvent laws of the State, was not entitled to priority under the Bankrupt Law; but the decision was rested solely upon the ground that the specific provisions of the Bankrupt Act concerning labor claims were intended to override the provisions relating to wages made by the State statute. That the exemption accorded by the State statute would have been valid in the absence of the express provisions of the Bankrupt Act concerning wages was conceded. The Bankrupt Act makes no such specific provision for debts due to States, Counties, and municipalities, and hence, by reference, adopts the statute of Massachusetts as part of its own provisions."

In re Lewis, 4 A. B. R. 51, 99 Fed. 935 (D. C. Mass.): "It has been held that State Laws, giving priority to wages, though included in the terms of § 64b, cl. 5, are yet ineffectual, because the whole matter of wages is dealt with and regulated by § 64b, cl. 4. * * * In other words, although the laws of a State giving priority to certain debts are by § 64b, cl. 5, introduced into the scheme of the present Bankrupt Act, yet such State laws are so introduced only so far as the debts to which they give priority are not expressly dealt with as to priority in the Bankrupt Act itself. Where both a State law and the Bankrupt Act give priority to the same class of debts, the Bankrupt Act not only controls the State law in the case of absolute conflict between the two, but, by its express regulation of these priorities, excludes the State law altogether."

Obiter, *In re Jones*, 18 A. B. R. 214, 151 Fed. 108 (D. C. Mich.): "It would also no doubt apply to bankrupt estates, but for the fact that the Bankrupt Act contains express provisions on the subject of preferences for labor debts which override the provision of the statute law."

§ 2204. Landlord's Priorities.—In the event of the impounding of an insolvent debtor's assets, in several states the landlord is entitled to priority of payment therefrom, to a certain extent, varying in the different states. The question arises, however, whether, in most instances, it is not a specific lien on the tenant's goods that the landlord possesses, rather than a mere claim for priority.⁶⁹

Thus, the landlord in Delaware is entitled to priority of payment out of the proceeds of property seized from the tenant's premises by legal proceedings and is so entitled to priority under § 64 (b) (5);⁷⁰ likewise, in

69. See discussion, ante, §§ 663, 664, 665, 1160, 1437, 1444, 2188; also, compare, *In re Consumers Coffee Co.*, 18 A. B. R. 500, 151 Fed. 933 (D. C. Pa.);

also, compare, *In re Bishop*, 18 A. B. R. 635, 153 Fed. 304 (D. C. S. Car.).

70. *In re Mitchell*, 8 A. B. R. 335, 116 Fed. 87 (D. C. Del.).

Pennsylvania,⁷¹ in Louisiana,⁷² and in Kentucky,^{72a} but in Kentucky not for future rent after bankruptcy.⁷³ And he has priority or rather a lien, in Iowa,⁷⁴ although in Iowa it is waived by the taking of a mortgage and the commingling of rent with other payments.⁷⁵

Likewise, the landlord has priority in West Virginia;⁷⁶ and his priority takes precedence of all liens created after the beginning of the tenant's term, and whether distress warrant be issued or not.⁷⁷

But in Maryland he is not entitled to priority unless he distrain before bankruptcy.⁷⁸

71. *Wilson v. Penna. Trust Co.*, 8 A. B. R. 169, 114 Fed. 742 (C. C. A. Pa.); *In re Duble*, 9 A. B. R. 121, 117 Fed. 795 (D. C. Pa.); *In re Hayward*, 12 A. B. R. 264, 130 Fed. 720 (D. C. Pa.); *In re Gerson*, 2 A. B. R. 170 (D. C. Pa.); *In re Goldstein*, 2 A. B. R. 603 (Ref. Pa.), even for rent in advance. *In re Hoover*, 7 A. B. R. 330, 113 Fed. 136 (D. C. Pa.); *In re Belknap*, 12 A. B. R. 326, 129 Fed. 646 (D. C. Penna.); *In re Lines*, 13 A. B. R. 318, 133 Fed. 803 (D. C. Pa.); compare, *In re Ruppel*, 3 A. B. R. 233, 97 Fed. 778 (D. C. Pa.). But compare, *In re Wheatlon Restaurant Co.*, 16 A. B. R. 294, 143 Fed. 921 (D. C. Pa.).

In re Ketterer Mfg. Co., 20 A. B. R. 694, 162 Fed. 583 (D. C. Pa.); compare, *In re Consumers Coffee Co.*, 18 A. B. R. 500, 151 Fed. 933 (D. C. Pa.); *In re Morris*, 19 A. B. R. 781, 156 Fed. 597 (D. C. Pa.); compare, *In re Piano Forte Mfg. Co.*, 20 A. B. R. 899, 163 Fed. 413 (D. C. Pa.); *In re Pittsburg Drug Co.*, 20 A. B. R. 227, 164 Fed. 482 (D. C. Pa.); compare, *In re West Paper Co.*, 20 A. B. R. 660, 162 Fed. 110 (C. C. A. Pa.); instance, *In re DeLancey Stables Co.*, 22 A. B. R. 406, 170 Fed. 860 (D. C. Pa.); *In re Keith-Gara Co.*, 29 A. B. R. 466, 203 Fed. 585 (D. C. Pa.).

No lien for rent nor priority to landlord in Pennsylvania out of proceeds of sale of liquor license, such property not being subject to distraint nor execution. *In re Myers*, 4 A. B. R. 536, 102 Fed. 869 (D. C. Pa.).

Exempt property: Landlord's lien: Without levy the landlord is entitled to his lien in Pennsylvania, at the hands of the bankruptcy court even though the property is otherwise exempt—exemptions being waived in the lease. *In re Sloan*, 14 A. B. R. 438, 135 Fed. 873 (D. C. Pa.).

Covenant that on default of one installment, all become due, causes all rent to become entitled to the priority. *In re Pittsburg Drug Co.*, 20 A. B. R. 227, 164 Fed. 482 (D. C. Pa.); but if the

landlord stands by and permits a sale in bulk of all fixtures, etc., and accepts purchaser as tenant, etc., he will not be allowed priority out of the commingled proceeds. *Vollmer v. McFadgen*, 20 A. B. R. 540, 161 Fed. 914 (C. C. A. Pa.), affirming *In re McFadgen*, 19 A. B. R. 481, 156 Fed. 715; also, *In re McFadgen*, 19 A. B. R. 481, 156 Fed. 715 (D. C. Pa.).

Payment of Taxes and Water Rent.—Payment of taxes and water rent, etc., where made part of the rent are included in the lien, if definite. *McCann v. Evans*, 26 A. B. R. 47, 185 Fed. 93 (C. C. A. Pa.). But not where the covenant to pay the water tax is separate and not a part of the rent. *In re Family Laundry Co.*, 27 A. B. R. 517, 193 Fed. 297 (D. C. Pa.).

72. *In re Meyer & Bleuler*, 28 A. B. R. 17, 195 Fed. 653 (D. C. La.); *Carriage Co. v. Solanas*, 6 A. B. R. 221, 108 Fed. 532 (D. C. La.).

But the lien does not, in Louisiana, at any rate, cover rent accruing after legal levy since the chattels are held no longer to be on the premises by the owner's consent. *Carriage Co. v. Solanas*, 6 A. B. R. 221, 108 Fed. 532 (D. C. La.).

72a. *In re Falls City Shirt Mfg. Co.*, 3 A. B. R. 437, 98 Fed. 592 (D. C. Ky.); *In re Byrne*, 3 A. B. R. 268, 97 Fed. 762 (D. C. Ky.).

73. *In re Jefferson*, 2 A. B. R. 208, 93 Fed. 948 (D. C. Ky.).

74. *In re Byrne*, 3 A. B. R. 268, 97 Fed. 762 (D. C. Ky.); *In re Hersey*, 22 A. B. R. 860, 171 Fed. 1001 (D. C. Iowa).

75. *In re Wolf*, 3 A. B. R. 558, 98 Fed. 74 (D. C. Iowa).

76. *In re McIntyre*, 16 A. B. R. 80, 142 Fed. 593 (D. C. W. Va.).

77. *In re McIntyre*, 16 A. B. R. 80, 142 Fed. 593 (D. C. W. Va.).

78. *In re Chaudron & Peyton*, 24 A. B. R. 811, 180 Fed. 841 (D. C. Md., disapproving *In re Rose*, 20 Fed. Cases 1176).

In Alabama the landlord has a lien for all future accruing rent under a lease, extending even to personal property sold at retail, and he will be entitled to an equitable lien on the proceeds where the selling at retail is without his knowledge;⁷⁹ but the lien on the proceeds is an equitable lien and where the trustee in bankruptcy sells the lease and the purchaser gives a sufficient bond, the landlord may be relegated to the purchaser.⁸⁰

Likewise, in South Carolina, the landlord has the old common-law right of distraint, but since the bankruptcy prevents levy thereof, such levy is considered as dispensed with.⁸¹

Similarly, the landlord has priority in Texas for rent due and becoming due for the current contract year, and this priority will be respected in bankruptcy.⁸²

The landlord is entitled to priority by way of lien in Georgia.⁸³

The costs and expenses of sale and only such may first be deducted from the proceeds of sale before payment of the lien.^{83a}

§ 2205. Priorities for Furnishing Supplies and Materials for Manufacturing Establishments: Fiduciary Debts as Guardian: Community Property of Husband and Wife, etc.—There are various other claimants entitled to priority on the distribution of an insolvent's estate under state law, whose rights have been passed upon in bankruptcy. Thus have been considered the priority of those furnishing materials or supplies for manufacturing establishments in various states;⁸⁴ and the effect of accepting a note therefor,⁸⁵ and of an assignment of the claim.⁸⁶

A fiduciary debt due from the bankrupt as guardian in Kentucky is entitled by statute to priority of payment on distribution regardless of inability to trace the trust funds, and it has the same priority in bankruptcy;⁸⁷

79. In re Varley & Bauman Co., 26 A. B. R. 104, 188 Fed. 761 (D. C. Ala.).

80. In re Varley & Bauman Co., 26 A. B. R. 104, 188 Fed. 761 (D. C. Ala.).

Landlord's Lien, on Sale of Leasehold—When Landlord Relegated to Rights Against Purchaser in Lieu of Lien or Proceeds of Sale of Property on Premises.—In one case the court, under the circumstances of the case, denied the landlord payment of his lien out of the proceeds of the sale of the personal property on the premises, and relegated him to his rights against the purchaser of the leasehold. In re Varley & Bauman, 26 A. B. R. 104, 188 Fed. 761 (D. C. Ala.).

81. In re Bishop, 18 A. B. R. 635, 153 Fed. 304 (D. C. S. Car.), quoted at § 2200.

82. Martin v. Orgain, 23 A. B. R. 454, 174 Fed. 772 (C. C. A. Tex.).

83. In re Burns, 23 A. B. R. 642, 175 Fed. 633 (D. C. Ga.). See, In re V. D.

L. Co., 23 A. B. R. 643, 175 Fed. 635 (D. C. Ga.).

83a. Compare ante, § 1992.

84. In re West Norfolk Lumber Co., 7 A. B. R. 648, 112 Fed. 767 (D. C. Va.); Mott v. Wissler Mfg. Co., 14 A. B. R. 321, 135 Fed. 697 (C. C. A. Va.); In re Falls City Shirt Mfg. Co., 3 A. B. R. 437, 98 Fed. 592 (D. C. Ky.); In re Bennett, 18 A. B. R. 320, 153 Fed. 673 (C. C. A. Ky., affirming 18 A. B. R. 847, 153 Fed. 673); In re Starks-Ullman Saddlery Co., 22 A. B. R. 596, 171 Fed. 834 (C. C. A. Ky.). Compare (lien, however, and not a "priority"), In re Monroe Lumber Co., 24 A. B. R. 371 (D. C. Miss.), quoted at § 1155, note.

85. In re Bennett, 18 A. B. R. 320, 153 Fed. 673 (C. C. A. Ky. App., 18 A. B. R. 847, 153 Fed. 673).

86. In re Bennett, 18 A. B. R. 320, 153 Fed. 673 (C. C. A. Ky.).

87. In re Crow, 7 A. B. R. 545, 116 Fed. 110 (D. C. Ky.).

but not so in Michigan, because it is not conferred as a general right of priority there.⁸⁸

Again, the bankruptcy law preserves the priority of community creditors upon community property of husband and wife, where that species of property right exists.⁸⁹

It has been held that because the peculiar laws of Louisiana permit an insolvent husband to pay back the "dation en paiement" to his wife, such payment not being considered fraudulent, therefore such payment is good in bankruptcy though made within the four months, as being a "priority" under § 64 (b) (5).⁹⁰ But such use of the term "priority" is unwarranted. "Priority" doubtless means simply a right to payment before others out of an insolvent's estate upon its seizure and distribution. This case seems to have been either a clear case of "preference" under § 60 although not a "fraudulent" transfer; or, perchance, it should be considered rather as the recognition of a species of "dower" right.

DIVISION 4.

DIVIDENDS TO GENERAL CREDITORS.

§ 2206. **Dividends to General Creditors.**—Whatever is left after costs, expenses and priority claims have been paid in full, is to be paid in dividends of equal percentum to general creditors.⁹¹

§ 2207. **To Be Paid in Two Dividends.**—The fund thus left for general creditors is to be divided into not less than two dividends:

The first dividend must not exceed half of what would be left for general creditors, after payment of costs and priority claims and after making allowance for costs, expenses and priority claims that probably will thereafter be allowed.

The final dividend is not to be declared until three months after the first dividend shall have been declared.⁹²

88. In re Jones, 18 A. B. R. 206 (D. C. Mich.).

89. In re Chavez, 17 A. B. R. 641, 149 Fed. 73 (C. C. A. N. Mex.): Here, however, the question again arises as to whether this is a right of priority merely or a lien.

90. Gomila v. Wilcombe, 18 A. B. R. 147, 151 Fed. 470 (C. C. A. La.). Compare, ante, § 2188.

91. Bankr. Act, § 65 (a): "Dividends of an equal per centum shall be declared and paid on all allowed claims, except such as have priority or are secured."

Meaning of Dividends as Construed before Amendment of 1903.—As to meaning of word "dividends" as a basis for figuring the commissions of the referee and trustee under the law before its amendment in 1903, see: In

re Hinckel Brewing Co., 10 A. B. R. 692, 124 Fed. 702 (D. C. N. Y.); In re Muhlhäuser, 9 A. B. R. 80 (Ref. Ohio); In re Coffin, 2 A. B. R. 344 (Ref. Tex.); In re Gerson, 2 A. B. R. 352 (Ref. N. Y.); In re Barber, 3 A. B. R. 306, 97 Fed. 547 (D. C. Minn.). Compare, In re Goldsmith, 9 A. B. R. 419, 118 Fed. 763 (D. C. Tex.).

Preferred and Secured Creditors, on Surrender.—A creditor who surrenders a security held by him and proves his claim as an unsecured one, is to be considered a general creditor in this respect. Lacy v. Citizens Bank, 28 A. B. R. 433, 198 Fed. 484 (C. C. A. Mo.).

92. Bankr. Act, § 65 (b) added by amendment of 1903: "Provided, That the first dividend shall not include more than fifty per centum of the money of the estate in excess of the

And the final dividend may be declared, if the facts warrant it, four months after adjudication.⁹³

§ 2208. Purpose of Two Dividends Protection of Dilatory Creditors.—This provision and the preceding provision were introduced by the amendment of 1903. It had been found that the efforts of Congress to have bankruptcy proceedings expeditious had resulted in some instances in the estate being paid out too rapidly, so that frequently creditors who happened for some cause or other to be delayed in filing their claims, were left out. For this reason Congress prescribed that where there was a fund for distribution to general creditors there should always be at least two dividends made of it and that there should be at least three months between the first and last one. However, owing to the peculiar wording of the amended act, there is no hindrance to the declaration of a second dividend, provided it be not a “final” dividend, within a few days after the first dividend; nor is there anything to prevent such second dividend absorbing almost all the remaining fund. All that is requisite is that the final dividend be not declared until three months after the first dividend.

Not only claims already allowed but those to be allowed are to be taken into account in arriving at the proper dividend to be declared for the first dividend.

§ 2209. First Dividend.—The first dividend must be declared within thirty days after the adjudication if there is money in the estate and if the money is enough to pay five per cent. on claims already allowed after deducting costs and other priority claims.⁹⁴

§ 2210. Dividends within Thirty Days after Adjudication Required Only Where Money in Estate.—Of course, if the assets have not been converted into money, the rule that the first dividend must be paid within thirty days after the adjudication does not apply. It only applies where the assets have been converted into money, in whole or in part, in time for such dividend to be declared within thirty days after the adjudica-

amount necessary to pay the debts which have priority and such claims as probably will be allowed: And provided further: That the final dividend shall not be declared within three months after the first dividend shall be declared.”

^{93.} In re Eldred, 19 A. B. R. 52, 155 Fed. 686 (D. C. N. Y.), quoted at § 2214.

No Withholding of Creditor's Dividend Because of Misconduct Towards Purchaser.—Where a creditor repudiates agreement with a purchaser of the assets, nevertheless his dividends may not be withheld. In re Augusta Pottery Co., 21 A. B. R. 64, 163 Fed. 1011 (D. C. W. Va.).

^{94.} Bankr. Act, § 65 (b): “The first dividend shall be declared within thirty days after the adjudication, if the money of the estate in excess of the amount necessary to pay the debts which have priority and such claims as have not been, but probably will be, allowed equals five per centum or more of such allowed claims. Dividends subsequent to the first shall be declared upon like terms as the first and as often as the amount shall equal ten per centum or more and upon closing the estate. Dividends may be declared oftener and in smaller proportion if the judge shall so order.”

Also, see In re Eldred, 19 A. B. R. 52, 155 Fed. 686 (D. C. N. Y.).

tion; as, for instance, where the estate already has been converted into money by an assignee or receiver in the state court who has been obliged to turn over the proceeds to the bankruptcy trustee; also, where the assets have been sold by the bankruptcy receiver or trustee, as perishable property.

§ 2211. Subsequent Dividends.—Dividends subsequent to the first are to be declared upon like terms as the first and as often as the amount equals ten per cent. or more and upon closing the estate.

Dividends may be declared oftener and in smaller proportions if the judge shall so order.

It has been held that a meeting of creditors to declare a final dividend may be combined with a final meeting.⁹⁵

§ 2212. Dividends Need Not Be Returned because of Filing of Subsequent Claims.—Dividends once paid out need not be returned because of the filing of subsequent claims that would have prevented the declaring of so large a dividend had they been allowed beforehand.⁹⁶

§ 2213. Claims Subsequently Filed, to Receive Prior Dividends before New Dividend Declared.—Creditors filing claims, or having claims allowed, after the declaration of one dividend are entitled to that dividend first before another dividend is declared to all creditors.⁹⁷

§ 2214. Need Not Retain Funds until Expiration of Year's Limitation for Proving Claims.—Because creditors are not prohibited from proving claims until the expiration of a year after the adjudication, does not require the trustee to hold the funds until the expiration of the year, nor does it prevent the closing of the estate beforehand.⁹⁸

In *re Bell Piano Co.*, 18 A. B. R. 185 (D. C. N. Y.): "To say that a final dividend shall not be declared within three months after the first dividend is declared, does in my judgment, say by implication that a final dividend may be declared on the expiration of three months from the time of the first dividend. All creditors must have notice of the first meeting, and if the creditors who have not yet proved their claims do not then prove them they may then lawfully, as well as justly, be debarred from participation in the funds in hand when the final meeting is held."

In *re Eldred*, 19 A. B. R. 52, 155 Fed. 686 (D. C. N. Y.): "As the prior pro-

⁹⁵. In *re Smith*, 2 A. B. R. 648 (Ref. N. Y.).

⁹⁶. Bankr. Act, § 65 (c): "The rights of creditors who have received dividends, or in whose favor final dividends have been declared, shall not be affected by the proof and allowance of claims subsequent to the date of such payment or declarations of dividends."

⁹⁷. Bankr. Act, § 65 (c): "But the creditors proving and securing the allowance of such claims shall be paid dividends equal in amount to those already received by the other creditors if the estate equals so much before

such other creditors are paid any further dividends."

Compare practice, before the amendment of 1903 required two dividends, where not enough was left over to pay the subsequent creditors the first dividend because of the filing of attorney's fee bills meanwhile. In *re Scott*, 2 A. B. R. 324, 93 Fed. 418 (D. C. Tex.).

⁹⁸. In *re Stein*, 1 A. B. R. 662, 94 Fed. 124 (D. C. Ind.); In *re Coulter*, 30 A. B. R. 75, 206 Fed. 906 (D. C. Pa.). See ante, § 731.

visions of the act have made it necessary to declare a first dividend within thirty days after adjudication, if there are funds sufficient to do so, and as the statute has provided that creditors who are not diligent, are permitted only to share in the estate that remains, and not to interfere with the funds already divided, it would appear that the court has the power to make a final dividend and to approve of a final report at any time after four months have elapsed subsequent to adjudication, if the other conditions are present showing the estate to be apparently ready for the final accounting."

§ 2215. "Ten Days Notice" of "Dividends."—Ten days notice by mail must be given to all creditors of the declaration and of the time of payment of the dividend, unless the notice is waived in writing.⁹⁹

§ 2216. "Dividend Sheets."—Dividend sheets, in the form prescribed by the Supreme Court as No. 40, are to be made out by the referee, stating the names of creditors and the dividend payable to each, and delivered by the referee to the trustee for the latter to use as a guide in paying out dividends.

§ 2217. Unclaimed Dividends.—Dividends which remain unclaimed for six months after the final dividend has been declared are to be paid by the trustee into court.¹

Dividends remaining unclaimed for one year are, under the direction of the court, distributed to the creditors whose claims have been allowed but not paid in full, and after such claims have been paid in full, the balance will be paid to the bankrupt: Provided, that in case unclaimed dividends belong to minors, such minors have one year after arriving at majority to claim such dividends.²

§ 2217½. Surplus Returned to Bankrupt.—There is no special provision of the act requiring the return to the bankrupt of any surplus after payment of all claims in full, but such surplus is to be returned to him on general equity principles.³ Before any surplus, after payment in full of all claims, is returned to the bankrupt, however, it must be applied in payment of interest accruing on the claims after the filing of the bankruptcy petition.⁴

§ 2218. Contracting to Postpone One's Dividend to That of Other Creditors.—Creditors undoubtedly may, by contract or estoppel, postpone their own dividends to those of others; ^{4a} as, for instance, where, on reorganization of a corporation, the old creditors agree that, in case of failure of the new organization, they will postpone their dividends to those of subsequent creditors.

99. Bankr. Act, § 58 (5).

1. Bankr. Act, § 66 (a). *Johnson v. Norris*, 27 A. B. R. 107, 190 Fed. 459 (C. C. A. Tex.).

2. Bankr. Act, § 66 (b). *Johnson v. Norris*, 27 A. B. R. 107, 190 Fed. 459 (C. C. A. Tex.).

3. *Johnson v. Norris*, 27 A. B. R. 107, 190 Fed. 459 (C. C. A. Tex.).

4. *Johnson v. Norris*, 27 A. B. R. 107, 190 Fed. 459 (C. C. A. Tex.).

4a. See post, § 2220; also see *In re Paris Modes Co.*, 28 A. B. R. 470, 196 Fed. 357 (C. C. A. N. Y.).

§ 2218 $\frac{1}{2}$. **Interest.**—Interest on claims drawing interest is to be computed to the date of the filing of the bankruptcy petition; and on claims not drawing interest but falling due after the filing of the petition, a rebate shall be deducted to the date of such filing.⁵

Where a mortgagee or other lienholder is seeking to share in dividends after application of his security on his claim, the interest on his claim is to be restricted to that due at the date of the filing of the bankruptcy petition, though it is computable to the date of the payment where it is paid from the proceeds, notwithstanding the bankruptcy.⁶

Before any surplus is returned to the bankrupt it has been held that it must be applied in payment of interest on the claims accruing after the filing of the bankruptcy petition.⁷

SUBDIVISION "A."

ADJUSTING EQUITIES IN DIVIDENDS AMONG CREDITORS.

§ 2219. **Adjusting Equities in Dividends among Creditors.**—The various equities existing among general creditors, and between creditors and others in the dividends, may be determined and adjusted, in the order of distribution.⁸

§ 2220. **Postponing Dividends of Some Creditors to Others, Because of Equities.**—Under the power of the court to adjust the equities existing among general creditors, it has been held that the claims of creditors who, though not guilty of preferences voidable under the peculiar provisions of the Bankruptcy Act, have yet been guilty of conduct which, under the ordinary rules of equity, would make it inequitable for them to share in the dividends on an equality with other creditors, may be postponed to the claims of other creditors in the distribution of dividends.⁹

5. See ante, § 598.

6. *Obiter*, *Coder v. Arts*, 18 A. B. R. 513, 152 Fed. 943 (C. C. A. Iowa), quoted at § 1146.

7. *Johnson v. Norris*, 27 A. B. R. 107, 190 Fed. 459 (C. C. A. Tex.).

8. Bankr. Act, § 2 (7). Inferentially, *Greenhall v. Carnegie Trust Co.*, 25 A. B. R. 300, 180 Fed. 812 (D. C. N. Y.); instance, *In re Paris Modes Co.*, 28 A. B. R. 470, 196 Fed. 357 (C. C. A. N. Y.); inferentially, *In re L. M. Alleman Hardware Co.*, 25 A. B. R. 331, 181 Fed. 810 (C. C. A. Pa.), reversing 22 A. B. R. 871.

9. *In re Siegel-Hillman Dry Goods Co.*, 7 A. B. R. 351 (D. C. Mo., reversed in *Swarts v. Siegel*, 8 A. B. R. 689, 117 Fed. 13).

In re Royce Dry Goods Co., 13 A. B. R. 267, 133 Fed. 100 (D. C. Mo.): In this case it was suggested that the dividend on the claim of the president of the bankrupt corporation should be

subjected to the priority of the claim of a creditor who had been misled by the false statements of the president as to the assets and had suffered loss in consequence.

Compare, *In re Rochford*, 10 A. B. R. 608, 124 Fed. 182 (C. C. A. S. Dak.); *Washington v. Tearney*, 27 A. B. R. 651, 194 Fed. 830 (C. C. A. W. Va.); instance, *In re Paris Modes Co.*, 28 A. B. R. 470, 196 Fed. 357 (C. C. A. N. Y.).

Compare *Lacy v. Citizens Bank*, 28 A. B. R. 433, 194 Fed. 484 (C. C. A. Mo.), wherein the court rightly held that where upon adjudication of the bankrupt a bank voluntarily relinquished all claims under a chattel mortgage which had been withheld from record, there was no foundation whatever for the position that the bank's claim should be postponed until all creditors who had become such between the date of the mortgage and the date of its filing had been paid in full.

In *re Rude*, 4 A. B. R. 319, 101 Fed. 805 (D. C. Ky.): "In order to settle and distribute a bankrupt's estate, all questions necessary to the ascertainment of the amount to be paid to each party to the proceedings must be adjudicated and determined by the court."

Compare, as to limitations of rule, In *re Girard Glazed Kid Co.*, 14 A. B. R. 485, 136 Fed. 511 (D. C. Pa.): "This is a dispute that has nothing to do with the bankruptcy proceedings, nor with the ascertainment of the true amount of the claim. It is a controversy growing out of a transaction that took place between these two persons, before the petition was filed, and concerns a sum of money that came into Barbara Swartz's possession at that time, and has remained in her possession ever since. It is an independent controversy about the ownership of money that is not a part of the fund for distribution, and this court cannot take jurisdiction of the dispute and decide it in the roundabout manner that has been suggested. If Barbara Swartz has money in her possession that belongs to Clara Illingsworth *ex aequo et bono*, the proper tribunal is open for an appropriate suit. To take other money from the former and decree it to the latter in this proceeding, would be to confuse two distinct and separate suits, having nothing to do with each other. Of the action in bankruptcy, the District Court has jurisdiction; but it has no jurisdiction of a suit to recover from Barbara Swartz any excess of payments that she may have received under the agreement of January 20, 1903."

Thus, again, where certain of the private creditors of a husband who had become such before his failure and the selling out of his business under a composition arrangement to his wife, are subsequently paid in full by him, but without her knowledge, while acting as her manager, it was held that such creditors might not share on an equality with other creditors in the dividends.¹⁰ Thus, also, where a chattel mortgage was withheld from record by agreement, but no claim was made thereunder, the debt itself was held to be provable but subordinate to the claim of one from whom a loan was secured on representations made at the mortgagee's instance that the property was clear and free, the money being used to pay the mortgagee.¹¹ Again, where the holder of the bankrupt's note had received a preferential payment on account from the bankrupt, and the endorser had paid after the bankruptcy the balance due thereon, it was held that the bankruptcy court would adjust the equities by requiring the endorser to surrender the preference in the first instance rather than have the creditor surrender and then come upon the endorser to make up the deficiency.¹²

And the court, it has been held, may postpone the dividends of a creditor who has entered into a combination to hinder, delay and defraud the other creditors.

In *re Headley*, 3 A. B. R. 272, 97 Fed. 765 (D. C. Mo.): "Under all the authorities, this was a fraudulent combination and scheme, which should postpone the claim of said bank for the amount of said judgment against the bankrupt estate. The Bankrupt Law is administered upon lines of equity jurisprudence, and, as

10. In *re Knox*, 3 A. B. R. 371, 98 Fed. 585 (D. C. N. Y.).

11. In *re Ewald & Brainard*, 14 A. B. R. 267, 135 Fed. 168 (D. C. Iowa).

12. In *re Seigel-Hillman Dry Goods Co.*, 7 A. B. R. 351 (D. C. Mo., reversed in *Swarts v. Siegel*, 8 A. B. R. 689, 117 Fed. 133).

between contending creditors, the bankrupt court, in the interest of fair dealing and good conscience, has the unquestioned power to postpone the claim of such a creditor in favor of the other creditors."

Undoubtedly, also, certain creditors could by contract or estoppel cause their claims to be subordinated to other creditors, even to other unsecured creditors.¹³

But the court has refused to give creditors whose debts had been assumed by the bankrupt a preference out of the proceeds of the property transferred by the original debtor to the bankrupt as consideration for the transfer.¹⁴

So, dividends may be withheld from one against whom the estate has an equitable set-off for unpaid stock subscriptions.

Kiskadden v. Steinle, 29 A. B. R. 346, 203 Fed. 375 (C. C. A. Ohio): "What, then should be done with the claim of Steinle? We have felt bound under the present record to assume that Bauman is solvent. If the claim be allowed and permitted now to share in the assets, according to the undisputed statement of counsel for appellee, Steinle would receive a sum nearly equal to the amount found by the referee to be due from Bauman upon his subscription. Still, if Bauman could meet his unpaid balance, not to speak of the liability of any of his co-stockholders, no ultimate loss to the other creditors would ensue. If, on the other hand, Bauman should not be able to pay anything remaining due on his subscription, Steinle (who stands no better than Bauman) would profit at the expense of the other creditors. In the latter event, however, the reasons for denying the set-off (or at least its equivalent in the nature of an equitable defense) against the Steinle claim would cease; for nothing would be gained by suit upon the subscription, and so nothing could be lost by the general creditors by applying whatever sum is really due from Bauman toward payment of the Steinle claim. *Rolling Mill Co. v. Ore & Steel Co.*, 152 U. S. 615, 616. Since it would be obviously inequitable to permit the Steinle claim to share ratably in the assets before properly disposing of the question of Bauman's obligation and his ability to pay it (*In re Goodman Shoe Co.* (D. C., Pa.), 3 Am. B. R. 200, 96 Fed. 949, 950, and *In re Duryea Power Co.* (D. C., Pa.), 20 Am. B. R. 219, 159 Fed. 783, 784, the underlying principles of which we regard as applicable), we are constrained to hold that the order of the court below allowing the claim should be reversed with costs; that all proceedings upon the Steinle claim be stayed, and all dividends that would accrue on such claim if allowed be withheld and preserved, until the Bauman debt and its availability be finally settled. If such debt be collected by the trustee, Steinle's claim shall be allowed in full; if by reason of his insolvency Bauman's debt is not collectible in whole or in part, Steinle's claim shall be accordingly reduced and the remainder allowed."

§ 2221. Thus, Dividing Fund, on Setting Aside Void Transfer, Solely among "Subsequent" Creditors.—Likewise, it has been held that the court may divide the fund among subsequent creditors to the exclusion of antecedent creditors, where an unrecorded chattel mortgage is void by the state law only as to subsequent creditors.¹⁵

¹³. See ante, § 2218. *In re Paris Modes Co.*, 28 A. B. R. 470, 196 Fed. 720, 153 Fed. 485 (D. C. Pa.).

¹⁵. *In re Cannon*, 10 A. B. R. 64, 357 (C. C. A. N. Y.). 121 Fed. 582 (D. C. S. C.).

¹⁴. *In re Baumblatt*, 18 A. B. R.

But this is dependent on state law; and in one state where a transfer has been set aside the setting aside has been held to redound to the benefit of all creditors, not simply to the benefit of those as to whom it was void.¹⁶

And it has been held under the Amendment of 1910, that inasmuch as the trustee's rights and remedies as a "creditor armed with process," are derived directly from the statute and not from the creditors of the estate, upon the setting aside of an unrecorded instrument by the trustee under § 47a (2), the division of the proceeds should be alike to all creditors whether prior or subsequent.¹⁷

§ 2222. Requiring Surrender of Illegal Advantage before Allowing to Share in Dividends.—The court, it has been held, may require the surrender of an illegal advantage obtained by one creditor over others before allowing his claim to share in the dividends.¹⁸

And in the same case it was held that this is so, although the debt sought to be allowed is a different one from that upon which the illegal advantage accrued.

§ 2223. Requirement of Surrender of Preferences before Allowing to Share in Dividends.—The court also has power expressly conferred by § 57 of the act not to allow a creditor who has received a preference voidable under § 60 to share in dividends until the preference is surrendered. This subject however, has been treated in extenso in previous parts of this treatise.¹⁹

16. See ante, § 1225½; also, *In re Kohler*, 20 A. B. R. 89, 159 Fed. 871 (C. C. A. Ohio).

17. *In re Farmers' Co-Op. Co. of Barlow No. 2*, 30 A. B. R. 190, 202 Fed. 1008 (D. C. N. Dak.), quoted at § 1225¾. See § 1225¾ for further discussion and cases on this proposition.

18. *In re Chaplin*, 8 A. B. R. 121, 115 Fed. 162 (D. C. Mass.): In this case a debtor, entering into a composition before bankruptcy with his creditors, secretly paid one of them more than the amount stated in the composition; the court held the preference so given to be fraudulent and voidable for two reasons; (1) because the transaction was an oppression of the debtor by the creditor; (2) because it was a fraud committed by both the debtor and the preferred creditor upon the other creditors ignorant of the preference; and the court further held that, on subsequent bankruptcy, such preference should not be treated as a set-off either to reduce the preferred creditor's claim or against the dividend to be received thereon, but must be

surrendered before the creditor could prove an independent debt.

Instance, but case reversed on facts, *In re Kessler & Co.*, 23 A. B. R. 391, 174 Fed. 906 (D. C. N. Y.), involving retention of stock paid for by a non-bankrupt who had gone into a separate joint stock enterprise with bankrupt.

Compare, *In re Knight, etc., Co.*, 26 A. B. R. 787, 190 Fed. 893 (D. C. Ala.): "Having secured the benefits of this settlement to the detriment of 'the trustee by asserting in the attachment suit that the cotton belonged to the bankrupt, they can not now be allowed to repudiate that position and assert ownership of the cotton in themselves for the purpose of claiming dividends on an equal basis with unpreferred creditors while retaining their preferences.'"

19. See ante, § 768. Instance, of voluntary surrender, *Lacy v. Citizens Bank*, 28 A. B. R. 433, 198 Fed. 484 (C. C. A. Mo.).

SUBDIVISION "B."

SUBJECTION OF DIVIDENDS BY GARNISHMENT AND EQUITABLE ACTION.

§ 2224. **Dividends Not to Be Subjected by Garnishment.**—The trustee may not be garnisheed for dividends in his hands.²⁰

Cowart v. Caldwell Co., 24 A. B. R. 546, 134 Ga. 544: "The general rule is that while property or money is in custodia legis, the officer holding it is the mere hand of the court; his possession is the possession of the court; to interfere with his possession is to invade the jurisdiction of the court itself; and an officer so situated is bound by the orders and judgments of the court whose mere agent he is, and he can make no disposition of such money or property without the consent of his own court, express or implied. Among the legal custodians to whom these principles have been applied are trustees or assignees in bankruptcy. * * * It has been held that even after the bill has been dismissed the receiver is still the officer of the court and not subject to garnishment."

Indeed, even after the court has declared the dividend or ordered the particular sum paid over, the trustee may not be garnisheed.

Cowart v. Caldwell Co., 24 A. B. R. 546, 134 Ga. 544: "It is contended, however, in the present case, that, inasmuch as the order of the referee directed the trustee to pay over the net proceeds of the sale to the W. E. Caldwell Company, it was thereby segregated and became a direct indebtedness or amount due to that company, and hence was subject to garnishment by its creditor. If a garnishment is served, a judgment rendered upon it against the garnishee must be upon it either against him in his individual capacity or in his official capacity, either against his personal funds or against the funds in his hands as trustee. This was not a transaction between James individually and the Caldwell Company, nor an individual indebtedness by him to that company, even though the company might have a right to proceed against him if he failed to pay it in accordance with the order of the court; for such right would arise out of the fact that he had not carried out such order. The garnishment recognizes the action of the court ordering the sale and the payment of the net proceeds as a valid order and is founded upon it. Without that order there would have been no sale and consequently no proceeds to pay. The garnishment proceeding, therefore, is necessarily against the trustee in his representative capacity, and is an effort to subject funds which he holds in that capacity under an order of the referee or bankruptcy court. That court has exclusive jurisdiction in matters of bankruptcy; the State court has none. In the regular order of proceedings, after distribution has been made, the bankrupt will seek a discharge, and the trustee, upon filing his report and account and vouchers, will also apply for a discharge. The court of bankruptcy will hardly grant him a discharge from his trust so long as he had money in his hands arising under an order of the court, not finally paid out or disposed of as the court had directed. If a State court could garnishee a trustee in bankruptcy, to catch funds in his hands which had been ordered paid by the court to which he was directly amenable, but which he had not actually paid out, and could compel him to withhold the pay-

²⁰ In *re Argonaut Shoe Co.*, 26 A. B. R. 584, 187 Fed. 784 (C. C. A. Cal.); In *re Hollander*, 25 A. B. R. 48, 181 Fed. 1019 (D. C. Md.). Compare In *re*

Charles Kranich, 25 A. B. R. 50, 182 Fed. 849 (D. C. Pa.), wherein the trustee made no objection to the garnishment, and it was allowed *ex gratia*.

ment, regardless of the order of the court of bankruptcy, it will be readily perceived that confusion and conflicts of jurisdiction would at once arise, and that a State court, by means of a garnishment, could indefinitely delay the final winding up of the matter in bankruptcy and the final discharge of the trustee. It has accordingly been held that a garnishment will not lie from a State court to a trustee or assignee in bankruptcy, to catch dividends which have been declared in favor of certain creditors or the amount which will be going to them under a composition. In *re Cunningham* (Dist. Court of Iowa), 9 Cent. Law J. 208; *Loveland on Bankruptcy*, § 268, p. 782; 2 *Remington on Bankruptcy*, §§ 2224, 2225, p. 1363. As the garnishment, in so far as it was directed to and served upon James as trustee in bankruptcy of the estate of Bailey, was without authority of law and void, and in so far as it was directed to and served upon him in his individual capacity it failed to reach and fasten upon any property or asset belonging to the defendant, no lawful levy of the attachment was made; and consequently the court was without jurisdiction of the attachment proceeding, and therefore properly dismissed it."

The dividend does not belong to the creditor until it is paid to him.²¹

Savings Bank v. Alden, 19 A. B. R. 886, 68 Atl. (Me.) 863: "But inasmuch as it is uniformly held by all courts that, in the absence of special statutory provisions to the contrary, money which is properly said to be in custodia legis cannot be reached by the process of foreign attachment, the question more specifically stated is whether a fund in the situation existing at the time of the service of the process in this case is still in the custody of the law, or whether, after distribution is ordered, and the checks are drawn and countersigned, but not delivered, the money has ceased to be in the possession of the court, or in the custody of the law. The plaintiff contends that the final order for distribution had been given by the United States court, that the purpose of the legal custody had been accomplished, that nothing further remained to be done by that court, and that the money cannot now be properly considered as in the custody of the law. The decisions in the Federal courts have uniformly recognized the doctrine that funds thus situated belonging to a bankrupt estate are in the custody of the law, and not amendable to process of foreign attachment against the trustee in bankruptcy. * * * Numerous decisions may be found in the State courts holding that funds in the hands of executors and administrators are subject to the trustee process; but it will be found that they are controlled by special statutory provisions, or influenced by considerations not applicable to the case at bar."

Nor is the garnishment bettered by garnisheeing the trustee individually; for he does not hold the funds individually, even after ordered to pay them over.²²

§ 2225. But Probably May Be by Equitable Action.—But probably dividends may be subjected by equitable action wherein a receiver is ap-

21. [1867] In *re Cunningham*, 19 N. B. Reg. 276; [1867] In *re Chisholm*, 4 Fed. 526; [1867] *Gilbert Ve Quimby*, 1 Fed. 111; [1867] In *re Kohlsaatt*, 18 N. B. Reg. 570; [1867] In *re Bridg-ham*, Fed. Cas. No. 1866; *Jackson v. Miller*, 9 Nat. Bankr. Reg. 143; *Cowart v. Caldwell Co.*, 24 A. B. R. 546, 134 Ga. 544, quoted this same action, §

2224; In *re Thompson-Breese Co.*, 30 A. B. R. 105 (Sp. M. Ohio); In *re American Electric Telephone Co.* [*Grant v. Burns*], 31 A. B. R. 612, 211 Fed. 88 (C. C. A. Ills.).

22. *Cowart v. Caldwell Co.*, 24 A. B. R. 546, 134 Ga. 544, quoted at § 2224, ante.

pointed to apply to the bankruptcy court for the dividend.²³ However, the state court cannot bring the trustee before it for such purpose.²⁴ The receiver must go to the bankruptcy court.

§ 2226. But Bankruptcy Court No Jurisdiction to Entertain Such Action.—But the bankruptcy court will not entertain the action.²⁵

§ 2227. If Bankrupt Garnishee, Trustee to Respond.—Where the bankrupt was garnishee in a proceedings pending at the time of bankruptcy, the trustee may be required to respond, but only to the extent of dividends due the party;²⁶ and the garnishment proceeding may be stayed until the dividends can be ascertained.²⁷ The bankruptcy court retains jurisdiction however, and the state court can enforce its order only through application to the bankruptcy court.²⁸

SUBDIVISION "C."

ATTORNEY'S LIEN ON CLIENT'S DIVIDEND.

§ 2228. Bankruptcy Court Has Jurisdiction over Attorneys' Lien Claims.—Liens claimed by attorneys for services rendered in the bankruptcy proceedings, upon dividends coming to clients, may be adjudicated in the bankruptcy court.²⁹

§ 2229. Attorney's Right to Lien.—Probably an attorney in bankruptcy proceedings may assert a lien on his client's dividends, for services performed in relation thereto.³⁰

Presumably the right to such lien would not be determined by local law, as would be the case had the lien originated before bankruptcy, but would be regulated wholly by general bankruptcy practice.

But compare, *In re Baxter*, 18 A. B. R. 450, 154 Fed. 22 (C. C. A. N. Y.): "We should entertain no doubt that no lien existed, if it were not for the effect to be given to the statute of New York respecting attorney's liens. An attorney has a lien upon the papers of his client in his possession, and a lien upon the fund or judgment which he has recovered for those whose interests he has represented in the suit. But, in the absence of some statutory provision, he has no

23. (1867) *Jackson v. Miller*, 9 Nat. Bankr. Reg. 143.

24. *Akins v. Stradley*, 1 N. W. Rep. (N. S.) 609; [1867] *In re Cunningham*, 19 Nat. Bankr. Rep. 276.

25. Compare, analogously, *In re Girard Glazed Kid Co.*, 14 A. B. R. 485, 136 Fed. 511 (D. C. Pa.).

26. *In re St. Albans Fdy. Co.*, 4 A. B. R. 594 (Ref. Vt.).

27. *In re St. Albans Fdy. Co.*, 4 A. B. R. 594 (Ref. Vt.).

28. *In re St. Albans Fdy. Co.*, 4 A. B. R. 594 (Ref. Vt.).

29. *In re Rude*, 4 A. B. R. 319, 101 Fed. 805 (D. C. Ky.).

30. *In re Rude*, 4 A. B. R. 319, 101 Fed. 805 (D. C. Ky.). Compare, *Cowley v. R. R. Co.*, 159 U. S. 575; compare, *R. R. Co. v. Pettus*, 113 U. S. 127.

Attorney's Fee as Part of Mortgage or Mechanic's Lien.—As to attorney's fee claimed as part of mortgagee's lien, see *In re Roche*, 4 A. B. R. 369, 101 Fed. 956 (C. C. A. Tex.). Also, see ante, § 671.

As to attorney's fee claimed as part of lien on foreclosure of mechanics' lien in state court, see *In re Adamo*, 18 A. B. R. 180 (D. C. N. Y.).

lien upon the naked cause of action of his client. Indeed, the whole law of an attorney's lien rests upon the principle that he has secured the fruits of a litigation of which he ought not to be deprived by the unfair conduct of his client. But the courts have always recognized the right of the client to settle the controversy with the opposite party against the consent of his attorney, and, where this has been done after an action has been commenced, have repeatedly declared as in *Emma Silver Mining Co. v. Emma Silver Mining Co.* (C. C.), 12 Fed. 815, that the attorney's lien cannot stand in the way, unless the settlement was made for the purpose of depriving the attorney of his costs. The proposition has never been more plainly and concisely stated than by Judge Brewer, now Mr. Justice Brewer, in *Swanson v. Chicago Ry. Co.* (C. C.), 35 Fed. 638, where he said: 'It is unquestioned that parties to a lawsuit may settle and compromise their litigation without consulting their counsel; and that, in the absence of a statute giving the attorney a lien for his fees, courts will not intervene unless there has been collusion between the parties, and an attempt to defraud the attorney out of his fees.' Upon the argument of the case, we were disposed to regard the New York statute as one merely regulating practice in the courts of the State, but a more careful reading of the statute satisfies us that it was intended to have a wider application, and should be treated as one establishing a substantive right. As merely a practice act, it would not affect the present proceeding, which is essentially an application to the equity powers of the court, as the courts of the United States, when exercising equity jurisdiction, are not controlled by the procedure established by the statutes of the States. But there are many instances when an enlargement of equitable rights or remedies by a State statute may be administered by the federal courts sitting within the State. * * * The federal courts have treated the question of an attorney's lien as depending upon the effect of local laws. In *re Paschal*, 10 Wall. 483, 495, * * * *Central R. Co. v. Pettus*, 113 U. S. 116, etc." * * * The result of these decisions [of New York] is that the statute does not preclude a settlement between the parties made in good faith and not intended to deprive the attorney of his compensation; and, if the client prefers to abandon the action, or release his cause of action for a nominal consideration, he is at liberty to do so, and the lien becomes practically of no value to the attorney; but whatever is received as a consideration becomes a fund impressed with the lien in the hands of the opposite party."

Of course an attorney's lien upon his client's papers is valid in bankruptcy to the same extent that it is void elsewhere.^{30a}

^{30a}. In *re Brown & Fleming Co.*, 21 A. B. R. 662 (Ref. N. Y.). Although in case it is the bankrupt who is the client, it could hardly be inferred that the right of retention should be absolute.

DIVISION 5.

ADMINISTRATION AND DISTRIBUTION OF PARTNERSHIP AND INDIVIDUAL ASSETS AND DEBTS IN PARTNERSHIP AND IN INDIVIDUAL BANKRUPTCIES RESPECTIVELY.

SUBDIVISION "A."

ADMINISTRATION AND DISTRIBUTION IN PARTNERSHIP BANKRUPTCIES IN GENERAL.

§ 2230. **In General.**—In cases where partnerships are in bankruptcy the administration of the estate and the distribution of the assets follow rules of their own. Owing to the dual capacity of a member of a partnership, an anomalous condition exists. A partnership is an association of individuals, and yet in many of its relations is to be considered an entity. The members are in the bankruptcy court in two capacities, as partners and also as individuals. There are several distinct yet connected estates thrown together in one administration, and the creditors of each have their separate rights and at the same time have their rights to share in the surplus of the other's estate. It will be well, even at the risk of repetition, to lay down, separately, some of the rules relative to the administration of partnership bankruptcies.

§ 2231. **Where Partnership Bankrupt, Whether Individual Estates Brought in Though Individuals Not Adjudged Bankrupt.**—Whether or not the partners are adjudged bankrupt individually as well as partners, the individual estate of each member is nevertheless brought into the bankruptcy court for administration.³¹

Francis v. McNeal, 228 U. S. 695, 30 A. B. R. 244, affirming S. C., 26 A. B. R. 555, 186 Fed. 481 (C. C. A. Pa.): "Since *Dory on Accounts* was made more famous by *Lindley on Partnership*, the notion that the firm is an entity distinct from its members has grown in popularity, and the notion has been confirmed by recent speculations as to the nature of corporations and the oneness of any somewhat permanently combined group without the aid of law. But the fact remains as true as ever that partnership debts are debts of the members of the firm, and that the individual liability of the members is not collateral like that of a surety, but primary and direct, whatever priorities there may be in the marshaling of assets. The nature of the liability is determined by the common law, not by the possible intervention of the Bankruptcy Act. Therefore ordinarily it would be impossible that a firm should be insolvent while the members of it remained able to pay its debts with money available for that end. A judg-

31. Bankr. Act, § 6 (c). Also, see § 65. But compare, § 477½; *In re Latimer*, 23 A. B. R. 388, 174 Fed. 824 (D. C. Pa.), affirmed sub. nom. *Francis v. McNeal*, 26 A. B. R. 555, 186 Fed. 481, affirmed *Francis v. McNeal*, 228 U. S. 695, 30 A. B. R. 244; *In re R.*

F. Duke & Son, 29 A. B. R. 93, 199 Fed. 199 (D. C. Ga.); *In re Samuels & Lesser*, 30 A. B. R. 293, 207 Fed. 195 (D. C. N. Y.). Contra, *In re City Contracting & Bldg. Co.*, 30 A. B. R. 133 (D. C. Hawaii).

ment could be got and the partnership debt satisfied on execution out of the individual estates.

"The question is whether the Bankruptcy Act has established principles inconsistent with these fundamental rules, although the business of such an act is, so far as may be, to preserve, not to upset, existing relations. It is true that by § 1, the word 'person,' as used in the act, includes partnerships; that by the same section, a person shall be deemed insolvent when his property, exclusive, etc., shall not be sufficient to pay his debts; that by § 5a a partnership may be adjudged a bankrupt, and that by § 14a any persons may file an application for discharge. No doubt these clauses, taken together, recognize the firm as an entity for certain purposes, the most important of which, after all, is the old rule as to the prior claim of partnership debts on partnership assets, and that of individual debts upon the individual estate. Section 5g. But we see no reason for supposing that it was intended to erect a commercial device for expressing special relations into an absolute and universal formula,—a guillotine for cutting off all the consequences admitted to attach to partnerships elsewhere than in the bankruptcy courts. On the contrary, we should infer from § 5, clause c through g, that the assumption of the Bankruptcy Act was that the partnership and individual estates both were to be administered, and that the only exception was that in h, 'in the event of one or more, but not all, of the members of a partnership being adjudged bankrupt.'

"In that case, naturally, the partnership property may be administered by the partners not adjudged bankrupt, and does not come into bankruptcy at all except by consent. But we do not perceive that the clause imports that the partnership could be in bankruptcy, and the partners not. The hypothesis is that some of the partners are in, but that the firm has remained out, and provision is made for its continuing out. The necessary and natural meaning goes no further than that.

"On the other hand, it would be an anomaly to allow proceedings in bankruptcy against joint debtors from some of whom, at any time before, pending, or after the proceeding, the debt could be collected in full. If such proceedings were allowed, it would be a further anomaly not to distribute all the partnership assets. Yet the individual estate, after paying private debts, is part of those assets, so far as needed. Section 5f. Finally, it would be a third incongruity to grant a discharge in such a case from the debt considered as joint, but to leave the same persons liable for it considered as several. We say the same persons, for however much the difference between firm and member under the statute be dwelt upon, the firm remains at common law a group of men, and will be dealt with as such in the ordinary courts for use in which the discharge is granted. If, as in the present case, the partnership and individual estates together are not enough to pay the partnership debts, the rational thing to do, and one certainly not forbidden by the act, is to administer both in bankruptcy."

Dickas v. Barnes Tr., 15 A. B. R. 567, 140 Fed. 849 (C. C. A. Ohio): "For the appellants it is contended that the court, having refused to declare them bankrupts, had no authority to treat them and their property as if they were bankrupts. Although there are several assignments of error on each appeal, they all rest on this contention. The argument is that not being bankrupts they are not subject to the jurisdiction of the bankruptcy court; that the refusal to declare them bankrupts put an end to the authority of the court to retain control of their property for the purpose of the bankruptcy proceeding; and it is complained that the court by its order in effect denied to them the immunity to which they were entitled by reason of the provisions of the Bankruptcy Act. By § 4b wage earners and tillers of the soil are excepted from those who may

be adjudged involuntary bankrupts. And for our present purpose we think the other appellants, who committed no act of bankruptcy, might be regarded as standing on the same footing as those who by reason of their occupation were exempt from an adjudication of bankruptcy. It may be conceded that but for the relation of these parties to the partnership, the contention they make, would be supported by perfectly adequate reasons. But on account of that relation other conditions exist. One who combines with others in a partnership enterprise becomes bound for the payment of the partnership debts. As partner he shares the fortunes of the partnership. In certain circumstances it may become subject to the exercise of the powers of a court of bankruptcy where its resources will be gathered in to satisfy the claims of creditors. One of those resources is the liability of the partner, for which his individual property stands charged. It is true that by virtue of the rule in equity, as well as in bankruptcy, for the marshaling and distribution of assets, his individual property is first applicable to the payment of his private debts, if there be any; the surplus then becomes assets for the payment of the partnership creditors. These consequences of partnership are not derived from the Bankrupt Act, but from the general law; and a partner is not relieved from them by his exemption from an adjudication of bankruptcy. If bankruptcy does not supervene, they would be worked out by a court of general jurisdiction, and the partner would be a party, a necessary party, to the record so that its liability for the firm debts could be enforced. In the bankruptcy court the partner may be brought before the court for the same purposes. In order to reach his property for the payment of the firm debts, it must be ascertained what surplus there will be after paying his private debts. It is said, however, that this must be done in a State court. But however this might be if he were a stranger, the partner is not to be regarded as a stranger, but as a party to the bankruptcy proceedings; and the court had authority to take such proceedings as were necessary to ascertain what assets were available and to subject them to the requirements of the case before it."

In *re Wing Yick Co.*, 13 A. B. R. 757 (D. C. Hawaii): "Although a partnership may be adjudged bankrupt without adjudging the partners bankrupt, yet in such case both the partnership assets and the individual assets of the partners are administered by the trustee and marshaled to prevent preferences and secure the equitable distribution of the property of the several estates."

Obiter, In *re Meyer*, 3 A. B. R. 559, 98 Fed. 976 (C. C. A. N. Y.): "We are of the opinion that it is the scheme of these provisions to treat the partnership as an entity which may be adjudged a bankrupt by voluntary or involuntary proceeding, irrespective of any adjudication of the individual partners as bankrupt, and upon an adjudication to draw to the administration the individual estates of the partners as well as the partnership estate, and marshal and distribute them according to equity. The assets of the individual estates and the debts provable against them can be ascertained without adjudicating the individual partners bankrupt. The language does not require such an adjudication."

And it is especially true that the individual estates are brought in where the adjudication of the firm involved the question of its solvency.³²

Contra, In *re Bertenshaw*, 19 A. B. R. 577, 157 Fed. 363 (C. C. A.): "But, as we have seen, the Act of 1867 expressly provided that 'where two or more persons who are partners in trade shall be adjudged bankrupt'—the only way in which it provided for the adjudication of a partnership—'all the joint stock and property of the copartnership and also all the separate estate of each of the partners

³². *Francis v. McNeal*, 26 A. B. R. 555, 186 Fed. 481 (C. C. A. Pa., affirmed *Francis v. McNeal*, 228 U. S. 695, 30 A. B. R. 244).

shall be taken' and administered (14 Stat. 534, § 36), while the Act of 1898 has no such provision for the taking of the separate estates upon the adjudication of the partnership. On the other hand, the Act of 1898 provides for the adjudication of a partnership bankrupt without an adjudication of any of its partners bankrupt, while the Act of 1867 has no such provision. Again, the Act of 1898 expressly prohibits the administration of the partnership property, and by so much the more the administration of the individual property of unadjudicated partners without their consent, while the Act of 1867 contained no such provision. Thus, while the Act of 1867 expressly required the court which adjudged a partnership insolvent to take and administer the separate estates of the partners and thereby sustained the rule in *Amsinck v. Bean*, the Act of 1898 contains no such requirement, but forbids not only the administration of his individual estate, but the administration of the estate of the partnership without the consent of the unadjudicated partner (section 5h); so that the rule in *Amsinck v. Bean* is not only without support, but it is inhabited by the provisions of the Act of 1898, and cannot prevail under it. This conclusion is supported by the actual decision rendered in *Amsinck v. Bean*, and by the reason which the court gave for it. The decision was that the assignees in bankruptcy of the estate of a partner could not take and administer the property of the partnership, and the reason given for it was that, while there was a provision in the Act of 1867 for the administration of the individual estate of a partner upon the bankruptcy of the partnership, there was no provision for the administration of the partnership's estate upon the bankruptcy of an individual partner, and hence it could not be made. By the same mark, the court of bankruptcy cannot take and administer the individual estate of an unadjudicated partner upon an adjudication of the bankruptcy of the partnership under the Act of 1898, because, while there is a provision for the administration of the partnership estate upon the adjudication of a partner bankrupt in certain circumstances (§ 5c), there is no provision in that act for the administration of the individual property of an unadjudicated partner upon an adjudication of a partnership bankrupt, and there is an express prohibition of the administration of the partnership estate in such a case without the consent of the solvent partner (§ 5h), and by so much the more an inhibition of the administration of his individual estate without his consent, * * * and the conclusion is that a court of bankruptcy upon an adjudication of a partnership bankrupt may not draw to itself and administer without his consent the individual estate of a solvent partner who has not been adjudicated a bankrupt."

And an individual partner, not himself adjudicated bankrupt, may be required to transfer his individual interest in the firm property to the firm trustee.³³

But it has been held that a receiver or trustee of a partnership adjudged a bankrupt is not the receiver or trustee of the property of another unadjudicated partnership in which the members of the bankrupt partnership were also members, and that he has no more right to seize or to administer such property than he has to take and distribute the property of any other stranger.³⁴

33. In re *Latimer*, 23 A. B. R. 388, 174 Fed. 824 (D. C. Pa.).

34. *Fidelity Trust Co. v. Gaskell*, 28 A. B. R. 4, 195 Fed. 865 (C. C. A. Mo.).

§ 2232. And "Consent" Not Necessary.—It has been held, to be sure, that where an individual member is not also adjudged bankrupt or does not "consent," the adjudication of the partnership will not draw into the administration the individual estate;³⁵ nor even permit administration of the firm assets;³⁶ but these rulings arise from a misconception of the scope of § 5 (h): "Consent" is requisite only when it is sought to administer firm assets in an individual bankruptcy; certainly not when it comes to the administration of a bankrupt partnership itself. Clearly § 5 (h) so reads. Without the statutory provision the rule would necessarily be the same: for the firm would not be insolvent unless each and every member were also insolvent. No "consent" of the individual member is requisite in cases of partnership bankruptcies for administration either of firm assets or of individual assets.³⁷

Francis v. McNeal, 228 U. S. 695, 30 A. B. R. 244, affirming S. C., 26 A. B. R. 555, 186 Fed. 491 (C. C. A. Pa.): "On the contrary, we should infer from § 5, clause c through g that the assumption of the Bankruptcy Act was that the partnership and individual estates both were to be administered, and that the only exception was that in h, 'in the event of one or more, but not all, of the members of a partnership being adjudged bankrupt.'

"In that case, naturally, the partnership property may be administered by the partners not adjudged bankrupt, and does not come into bankruptcy at all except by consent. But we do not perceive that the clause imports that the partnership could be in bankruptcy, and the partners not. The hypothesis is that some of the partners are in, but that the firm has remained out, and provision is made for its continuing out. The necessary and natural meaning goes no further than that."

See dissenting opinion in *In re Bertenshaw*, 19 A. B. R. 577, 157 Fed. 363 (C. C. A.): "It is said this paragraph means that, when a partnership has been declared bankrupt and also one or more but not all of its members, the court has no power to administer the partnership estate without the consent of the non-bankrupt members. And the argument is that, as the court has no such power, much less has it the power when actually administering the partnership estate, to compel a non-bankrupt partner to bring in his individual property. But it is manifest that § 5h does not bear the construction given it. It deals with the bankruptcy of individual partners, not with the bankruptcy of the firm. If an individual partner becomes bankrupt, it becomes important to know the effect upon the firm of which he is a member. It not infrequently happens that a firm remains solvent and prosperous, though a member becomes insolvent and commits an act of bankruptcy not chargeable to or connected with the business of the partnership. The provision for such cases is found in the paragraph quoted, and it has nothing to do with the bankruptcy of the partnership. It recognizes, however, that before the bankrupt partner

35. Compare, § 65. *Strauss v. Hooper*, 5 A. B. R. 228, 105 Fed. 590 (D. C. N. Car.); *In re Bertenshaw*, 19 A. B. R. 577, 157 Fed. 363 (C. C. A.), but the dissenting opinion in this case seems to present the preferable rule.

36. *In re Blair*, 3 A. B. R. 580 (D. C. N. Y.); *In re Solomon & Carvel*, 20 A. B. R. 488, 163 Fed. 140 (D. C.

N. Y.); *In re Bertenshaw*, 19 A. B. R. 577, 157 Fed. 363 (C. C. A.), but the dissenting opinion presents the truer rule.

37. Compare post, §§ 2251, 2791. Contra, *In re City Contracting & Bldg. Co.*, 30 A. B. R. 133 (D. C. Hawaii).

receives a discharge his beneficial interest in the firm property, after the payment of firm debts, should be applied to the payment of his individual obligations. But, since his associates have an interest in the partnership property to which his individual creditors cannot look, they are justly given the preference in liquidating their joint affairs. Eventually, however, the net share of the bankrupt partner is brought into the individual proceedings. That a partnership may be an entity for certain purposes and its property its own does not prevent the bankruptcy of a single partner from resulting in a liquidation of the joint business, and the application of his net share therein to the payment of his individual debts. Rightly regarded the paragraph quoted suggests the true rule for the converse situation—the bankruptcy of the partnership and the nonbankruptcy of a member. There is, however, this distinction. In a case covered by § 5h, the nonbankrupt partner has no contractual connection with the debts of his bankrupt copartner. He is not liable for them, and should, therefore, suffer no loss or inconvenience, save what comes from a necessary winding up of the partnership as in other cases of dissolution. Therefore he is given the preference in the settlement of the firm business of which he is part owner. But these reasons do not apply in a case like the one before us. The nonbankrupt partner is liable for all the debts of his bankrupt firm, and the firm creditors may look to his property for satisfaction subject to equitable limitations in favor of his individual creditors. A court of equity, with all parties before it, partnership and members, grants full relief, and the law has not required it to intrust the administration of estates to resisting debtors."

§ 2233. Partnership Trustee, Trustee Also of Individual Estates.

—As previously noted,³⁸ the creditors of the partnership elect the trustee in partnership bankruptcies.

The trustee elected by the partnership creditors becomes, by virtue of his office, trustee of each of the individual estates of the several partners.³⁹ And this is so, even where the individual member is not himself, individually, a bankrupt.

Thus, even where an individual member is not himself a bankrupt, it has been held that his assignee may be ordered summarily to turn over the individual assets for administration in the partnership bankruptcy,⁴⁰ although this decision carries the rule too far, the nullification of the assignment being dependent upon the assignor's adjudication as bankrupt, and the state court retaining jurisdiction where he is not adjudged bankrupt.⁴¹

38. See ante, §§ 65, 477½, 866. Bankr. Act, § 5 (b): "The creditors of the partnership shall appoint the trustee." Obiter, *In re Eagles & Crisp*, 3 A. B. R. 733, 99 Fed. 696 (D. C. N. Car.).

39. Bankr. Act, § 5 (c): "The court of bankruptcy which has jurisdiction of one of the partners may have jurisdiction of all the partners and of the administration of the partnership and individual property."

In re Coe, 18 A. B. R. 715, 154 Fed. 162 (D. C. N. Y.), quoted at § 867½.

Contra, *In re City Contracting & Bldg. Co.*, 30 A. B. R. 133 (D. C. Hawaii).

40. *In re Stokes*, 6 A. B. R. 262, 106 Fed. 312 (D. C. Penna.).

41. But a lien suffered by a member of a bankrupt partnership to be taken on his individual property, by legal proceedings, within four months of the partnership, has been held not avoided by the partnership bankruptcy. *In re Lehigh Lumber Co.*, 4 A. B. R. 221, 101 Fed. 216 (D. C. Pa.).

At any rate the individual member may himself be ordered summarily to transfer his individual interest in property to the trustee for administration.⁴²

The court may, in its discretion, cause the election of separate trustees for the firm and its members, but this power will only be exercised in cases of special or peculiar necessity.⁴³

§ 2234. Separate Accounts to Be Kept and Joint Expenses Apportioned.—The administrations of the partnership estate, and of the several individual estates of the different partners, are to be kept distinct. Separate accounts are to be kept and joint expenses are to be apportioned.⁴⁴

§ 2235. Property Originally Individual, Becoming Partnership, to Be Administered as Such.—Property originally owned by one or more of the partners, and used in the partnership business, may be joint or separate estate, as may be agreed upon between the partners either in writing or by parol agreement.⁴⁵

§ 2236. Agreement Not Necessarily Express.—The parol agreement need not be express but may be proved by a course of conduct, as by entries upon the partnership books, or by circumstantial evidence.⁴⁶

Thus, real estate standing in one partner's name may be shown to be partnership property.⁴⁷

§ 2237. Partnership Debts "Provable" against Individual Both in Partnership and in Individual Bankruptcy, Likewise Individual Debts against Partnership.—Partnership debts are "provable" against the individual estates of the several members, either in partnership cases or in individual cases; and likewise individual debts are "provable" against the partnership share of the individual members either in partnership or individual cases: the priority of right to share in the particular fund does not affect the provability.

42. In re Latimer, 23 A. B. R. 388, 174 Fed. 824 (D. C. Pa.).

43. In re Currie, 28 A. B. R. 834, 197 Fed. 1012 (D. C. Mich.).

44. Bankr. Act, § 5 (d): "The trustee shall keep separate accounts of the partnership property and of the property belonging to the individual partners."

Bankr. Act, § 5 (e): "The expenses shall be paid from the partnership property and the individual property in such proportions as the court shall determine."

45. Instance of contribution to partnership enterprise evidenced in writing: Seat in stock exchange standing in one partner's name. In re Hurlbutt, 13 A. B. R. 50, 135 Fed. 504 (C. C. A. N. Y.).

Instance of facts insufficient to prove contribution: Seat in stock exchange; Burleigh v. Foreman, 12 A. B. R. 88, 130 Fed. 13 (C. C. A. Mass.).

In re Haring, 27 A. B. R. 285, 193 Fed. 168 (D. C. Mich.).

46. In re Swift, 9 A. B. R. 237, 118 Fed. 348 (D. C. Mass., reversed for insufficiency of facts, Burleigh v. Foreman, 12 A. B. R. 88, C. C. A.). Compare, analogously, In re Jones, 8 A. B. R. 626 (D. C. N. Car., reversed sub nom. Davis v. Turner, 9 A. B. R. 704, 120 Fed. 605, C. C. A.).

47. In re Mosier, 7 A. B. R. 268, 112 Fed. 138 (D. C. Vt.); In re Groetzing, 11 A. B. R. 723, 127 Fed. 814 (C. C. A. Penn., affirming 6 A. B. R. 399).

In re Hee, 13 A. B. R. 8 (D. C. Hawaii): "It is not necessary for the court to decide this point because it makes no difference as to their right of petitioning for the adjudication of L. Hee as a bankrupt, whether they were creditors of a partnership of which he was a member or whether they were creditors of L. Hee in his individual capacity, a partner of the partnership being liable for all the partnership debts."

Thus, partnership debts are provable in the individual bankruptcy of a member.⁴⁸

In re Bates, 4 A. B. R. 56, 100 Fed. 263 (D. Ct. Vt.): "* * * the individual assets may have been applied to individual debts to the exclusion of partnership debts till after the individual debts are all paid, and there may never be anything whatever to go to the partnership creditor; but his debt is none the less provable. Whether a debt is provable depends upon the nature of the liability, and not upon whether there are assets, or there is any prospect of assets, applicable to it. This partnership debt is a simple contract debt of the partnership, and a simple contract liability of the bankrupt, and the individual debt is a similar liability, and both are of the provable class."

In re Mercur, 2 A. B. R. 627, 95 Fed. 634 (D. C. Pa.): "The creditors of a partnership are also creditors of each individual member, and have a right to petition against him, as well as against the firm. This has been several times decided, and is supported by principle no less than by authority. How far the partnership creditors may be entitled to share in the distribution of the separate property of each member is a distinct question, which can only be determined hereafter when the assets come to be marshaled."

§ 2238. Partnership Creditors to Exhaust Partnership, Assets, Individual Creditors to Exhaust Individual Assets; Each to Share in Other Only in Surplus.—Partnership creditors have the right to be first paid in full out of the partnership assets before any other creditors; and individual creditors have the right to be first paid in full out of the respective individual estates before any other creditors; but the creditors of the partnership estate may, after exhausting the assets of the partnership estate share in any surplus of the individual estates left after paying the creditors of the individual: and vice versa.⁴⁹

48. Jarecki Mfg. Co. v. McElwaine, 5 A. B. R. 751, 107 Fed. 249 (C. C. Ind.); Loomis v. Wallblom, 13 A. B. R. 687, 94 Minn. 392; In re Kaufman, 14 A. B. R. 393, 136 Fed. 262 (D. C. N. Y.); impliedly, In re Hartman, 3 A. B. R. 65, 96 Fed. 593 (D. C. Iowa); impliedly, In re McFaun, 3 A. B. R. 66, 96 Fed. 592 (D. C. Iowa); Deaf & Dumb Institute v. Crockett, 17 A. B. R. 237, 117 N. Y. App. Div. 269.

49. Bankr. Act, § 5 (f): "The net proceeds of the partnership property shall be appropriated to the payment of the partnership debts, and the net proceeds of the individual estate of each partner to the payment of his individual debts. Should any surplus remain of the property of any partner after paying his individual debts, such

surplus shall be added to the partnership assets and be applied to the payment of the partnership debts. Should any surplus of the partnership property remain after paying the partnership debts, such surplus shall be added to the assets of the individual partners in the proportion of their respective interests in the partnership."

Bankr. Act, § 5 (g): "The court may permit the proof of the claim of the partnership estate against the individual estates, and vice versa, and may marshal the assets of the partnership estate and individual estates so as to prevent preferences and secure the equitable distribution of the property of the several estates."

In re Wilcox, 2 A. B. R. 117, 94 Fed. 84 (D. C. Mass.); In re Janes, 13 A.

In *re Stein & Co.*, 11 A. B. R. 536, 127 Fed. 547 (C. C. A. Ills.): "The present Bankruptcy Act recognized the equitable rule that partnership property is primarily a fund for the payment of copartnership debts, and that the interest of a copartner is subject to that special equity, and attaches only to the surplus remaining after the payment of the copartnership debts."

Vaccaro v. Security Bk., 4 A. B. R. 482, 103 Fed. 436 (C. C. A. Tenn.): "It is true that in equity the individual debts of a partner are entitled to be first paid out of the individual property and firm debts out of partnership property, but in each case the surplus, after providing for the preferred debt, is applicable to the payment of debts of the other class."

"This too is the order of payment prescribed by § 5 of the Bankrupt Act of 1898."

Obiter, *Buckingham v. First Nat. Bk.*, 12 A. B. R. 469, 131 Fed. 849 (C. C. A. Tenn.): "This is a statutory statement of a general rule early adopted in England (*Ex parte Crowder*, 2 Vernon 706), upon which, subsequently, an exception was engrafted to the effect that firm creditors may share in the individual assets in competition with individual creditors, if there be no firm assets and no solvent partner."

Jacobs v. Van Sickle, 10 A. B. R. 519, 123 Fed. 340 (D. C. N. J.): "Then, too, Kline may be assumed to know that in any bankruptcy proceedings, even if Van Sickle were a partner in Grant Bros., in the administration of the estates of the partnership and of the partners in bankruptcy the individual estate of each partner was primarily liable for the payment in full of his individual debts."

In *re Mosier*, 7 A. B. R. 269, 112 Fed. 138 (D. C. Vt.): "Partnership creditors

B. R. 341, 133 Fed. 912 (C. C. A. N. Y., reversing 11 A. B. R. 792); *Jarecki Mfg. Co. v. McElwaine*, 5 A. B. R. 751, 107 Fed. 249 (D. C. Ind.); In *re Denning*, 8 A. B. R. 133, 144 Fed. 219 (D. C. Mass.); inferentially, In *re Groetzinger*, 11 A. B. R. 723, 127 Fed. 814 (C. C. A. Pa., affirming 6 A. B. R. 399); Inferentially, In *re Corcoran*, 12 A. B. R. 283 (Ref. Ohio, affirmed by D. C.); In *re Hobbs & Co.*, 16 A. B. R. 548, 145 Fed. 211 (D. C. W. Va.).

In *re Blanchard*, 20 A. B. R. 417, 161 Fed. 793 (D. C. N. Car.); *Adams v. Deckers Lumber Co.*, 29 A. B. R. 42, 202 Fed. 48 (C. C. A. W. Va.); In *re Chandler*, 25 A. B. R. 865, 185 Fed. 1006 (C. C. A. Ill.); In *re Union Bank Co.*, 25 A. B. R. 148, 184 Fed. 224 (C. C. A. Mich.); In *re Effinger*, 25 A. B. R. 930, 184 Fed. 728 (D. C. Md.); *Johnson v. Norris*, 27 A. B. R. 107, 190 Fed. 459 (C. C. A. Tex.). Also, see post, § 2255.

This rule is said to apply only in cases where both the partnership and the individual estates are before the court for distribution. *Conrader v. Cohen*, 9 A. B. R. 619, 121 Fed. 801 (C. C. A. Penn., affirming In *re Conrader*, 9 A. B. R. 85, 118 Fed. 676).

Contra, In *re Wilcox*, 2 A. B. R. 117, 94 Fed. 84 (D. C. Mass.).

After the expiration of the year

within which claims may be filed, a creditor who holds a firm note with individual members' endorsements thereon, and who has proved the same solely against the partnership estate, will not be permitted to amend so as to prove them against the individual estates as well. In *re McCallum*, 11 A. B. R. 447, 127 Fed. 768 (D. C. Penn.).

This rule is said to be simply declaratory of the common rule of equity so far as concerns the right of partnership creditors to priority of payment out of firm assets, but to state a new rule as to individual creditors; for in equity partnership creditors have a lien on partnership assets for the payment of firm debts, but individual creditors have no such lien on individual assets.

In *re Mosier*, 7 A. B. R. 268, 112 Fed. 138 (D. C. Vt.): "Partnership creditors have a lien, in equity, upon partnership property for the payment of partnership debts. * * * But individual creditors have no lien at common law or in equity, upon individual property against partnership creditors for individual debts. That right is provided for by, and rests wholly upon, the Bankrupt Law." Inferentially, In *re Janes*, 13 A. B. R. 341, 133 Fed. 912 (C. C. A. N. Y.).

have a lien in equity, upon partnership property for the payment of the partnership debts. *Washburn v. Bank*, 19 Vt. 278. This right is expressly provided for in the Bankrupt Law. Section 5f. But individual creditors have no lien, at common law or in equity, upon individual property, against partnership creditors for individual debts. * * * That right is provided by, and rests wholly upon, the Bankrupt Law."

The rule obtains though the debt be a "priority" debt; thus the personal tax of a member of a partnership is not to be paid out of firm assets until firm creditors are satisfied in full.⁵⁰ And this rule applies even though the bankrupt firm is composed of individuals and another firm.⁵¹

But a creditor who, after his debt was incurred, became a partner of his debtor in a separate and distinct transaction, may prove his claim against the individual estate of the debtor, even to the diminution of the fund available for partnership creditors.⁵²

No "exceptions" are to be allowed to the rule; even where a partnership and all its members are adjudicated bankrupt in the same proceedings and there are no partnership assets but only individual assets—the individual creditors must nevertheless be first satisfied out of the individual estates and partnership creditors may only share in any surplus.⁵³

§ 2239. Section 5 Refers Only to Actual Partnerships, Not Those by "Holding Out."—The provisions of § 5 of the Bankruptcy Act refer only to cases of actual partnerships between the parties, not to partnerships that are merely such as to certain creditors by "holding out" or otherwise.⁵⁴

§ 2240. Obligations Signed by Firm Name, Prima Facie Allowable as Firm Debts.—Obligations signed by the firm in the firm name are prima facie allowable against the partnership estate.⁵⁵

Thus, an accommodation indorsement in the firm name made by one partner will bind the partnership in the hands of a bona fide holder.⁵⁶ Of course, however, where the holder had notice, actual or constructive, as for example where the note showed on its face that it was an accommodation indorsement, the holder would take subject to the possible defense of lack of power.

50. In *re Flatau & Stern*, 21 A. B. R. 352 (Ref. N. Y.).

51. In *re Knowlton & Co.*, 28 A. B. R. 140, 196 Fed. 837 (D. C. Pa.).

52. In *re John Strawbridge*, 25 A. B. R. 355 (Ref. Pa.).

53. In *re Janes*, 13 A. B. R. 341, 133 Fed. 912 (C. C. A. N. Y.); In *re Wilcox*, 2 A. B. R. 117, 94 Fed. 84 (D. C. Mass.).

54. Compare ante, §§ 57, 58, 60 and 63. In *re Kenney*, 3 A. B. R. 353, 97 Fed. 554 (D. C. N. Y., affirmed in 5 A. B. R. 355, 105 Fed. 897, itself affirmed in *Clarke v. Larrimore*, 188 U. S. 486); In *re Gibson*, 27 A. B. R. 401,

191 Fed. 665 (D. C. So. Dak.). Also see In *re Pinson & Co.*, 24 A. B. R. 804, 180 Fed. 787 (D. C. Ala.), quoted at §§ 45½, 57 and 58.

Instance held joint ventures but not partnership, *Mayes v. Palmer*, 31 A. B. R. 225, 208 Fed. 97 (C. C. A. Mo.).
"Universal" Partnerships.—Compare, In *re Culver*, 23 A. B. R. 779, 176 Fed. 450 (D. C. Minn.).

55. *Merchants' Bank v. Thomas*, 10 A. B. R. 299, 121 Fed. 306 (C. C. A. Miss.). Compare post, § 2245.

57. *Union Nat'l Bank v. Neill*, 17 A. B. R. 841 (C. C. A. Tex.).

§ 2241. Individual Debt Assumed by Firm Provable against Partnership if Sufficient Consideration.—The individual debt of a partner may be assumed by the firm, if sufficient consideration exists; and the debt in that instance will be a provable debt against the firm estate in bankruptcy.⁵⁸

Thus, notes of a new firm are given on sufficient consideration when given to pay the debts of individual partners equal to the value of the respective shares contributed by each.⁵⁹ Likewise, where a firm assumes all of one partner's assets and liabilities, the partner's individual liabilities become firm liabilities and are supported by sufficient consideration, and the transaction is not within the statute of frauds.⁶⁰ Again, a firm note given by both partners is a valid partnership debt where it is given for an existing business debt of the original partner, who had sold a half interest in his business on condition that the incoming partner assume half of such debt.⁶¹

Notes given by the firm to settle up a partner's embezzlement of government money are valid against the firm, where the embezzled money went to pay firm debts.⁶²

On the other hand, notes signed in the firm name by one partner and given by him to a bank in renewal of an individual indebtedness, the bank having knowledge, are not provable against the partnership estate in bankruptcy, where there is not sufficient evidence that the partnership had assumed the indebtedness.⁶³

§ 2242. But Assumption Must Be Acquiesced in by Creditor.—But the assumption by the firm must be with the knowledge and consent or acquiescence of the creditor, else the obligation remains individual.⁶⁴

Thus, the entry of an individual partner's debt on the firm books, unknown to the creditor, and payments thereon from time to time with firm checks, do not change the character of the debt to that of a firm obligation.⁶⁵

Again, a mortgage of partnership property, given by one partner to secure his individual indebtedness, even with the consent of the other partner, has been held not enforceable in bankruptcy against firm creditors.⁶⁶

But a sealed note in South Carolina does not bind the firm unless the act of both partners. *Pollock v. Jones*, 10 A. B. R. 616, 124 Fed. 163 (C. C. A. S. Car.).

^{58.} *Kelsey v. Munson*, 28 A. B. R. 520, 198 Fed. 841 (C. C. A. Colo.).

^{59.} *Merchants' Bk. v. Thomas*, 10 A. B. R. 299, 121 Fed. 306 (C. C. A. Miss.).

^{60.} *In re Dresser*, 13 A. B. R. 747, 135 Fed. 495 (C. C. A. N. Y.).

^{61.} *Dacovich v. Schley*, 13 A. B. R. 752, 134 Fed. 72 (C. C. A. Ala.).

^{62.} *In re Speer Bros.*, 16 A. B. R. 524 (D. C. Ore.).

^{63.} *First Nat'l Bk. of Miles City v. State Nat'l Bk.*, 12 A. B. R. 429, 131 Fed. 422 (C. C. A. Mont., affirming

In re McIntire, 12 A. B. R. 429).

^{64.} **Assumption of Corporate Debts on Buying Out Corporation.**—Where an individual bought out the assets of a corporation and assumed its debts and later formed a partnership which took over the same property and debts and later still became bankrupt, the original corporate creditors are firm creditors, not individual. *In re Sickman & Glenn*, 19 A. B. R. 232, 155 Fed. 508 (D. C. Pa.).

^{65.} *Hibberd v. McGill*, 12 A. B. R. 101, 129 Fed. 590 (C. C. A. Pa., affirming *In re Wiseman*, 10 A. B. R. 550, 123 Fed. 185). Inferentially, *In re Blanchard*, 20 A. B. R. 417, 161 Fed. 793 (D. C. N. Car.).

^{66.} *In re Blanchard*, 20 A. B. R. 417, 161 Fed. 793 (D. C. N. Car.).

§ 2243. Loan to Enable Partner to Furnish Contributory Share Not Firm Debt.—A loan made by a third party to enable one to furnish his contributory share to a partnership enterprise is not a firm debt.

Thus, loans by two fathers to set up their sons as partners in the same business, evidenced by notes signed by both sons in their respective individual names, were held not to be firm obligations, although the money went into the firm business.⁶⁷ And claims for advancements to further the firm enterprise of a partner in an illegal or ultra vires partnership, composed of a corporation and another partnership, may not be proved against the other partnership; and the corporation which was a de facto partner may not prove its advancements to the partnership enterprise as a debt against the partnership, on the theory that it was not a partner because of the ultra vires.⁶⁸ But its advances made prior to its entry into the ultra vires partnership to the other partners (the present bankrupts) may be proved against the other partners.⁶⁹

§ 2244. Mere Joint Obligations, Not Amounting to Partnership Debts, Not Allowable, on Par with Firm Debts.—Mere joint obligations, not amounting to partnership obligations, are not allowable against firm assets on a par with firm debts.^{69a}

In *re Weisenberg & Co.*, 12 A. B. R. 418, 131 Fed. 517 (D. C. Ky.): "It is certain that if, for either reason the notes in question must be treated as joint debts, they cannot be allowed as valid claims against the firm assets, on a par with firm creditors."

§ 2245. Parol Evidence Admissible to Show Obligations, Apparently Individual, to Be Firm Debts.—Parol evidence is admissible to show that obligations apparently individual are in reality firm debts.⁷⁰

67. *Strause v. Hooper*, 5 A. B. R. 225 (D. C. N. Car.).

Compare *Mock v. Stoddard*, 24 A. B. R. 403, 177 Fed. 611 (C. C. A. Idaho, distinguishing *Strause v. Hooper* supra): "In the case of *Strause v. Hooper* (D. C., N. C.), 5 Am. B. R. 225, 105 Fed. 490, it was held that notes signed by both members of a partnership for money borrowed and put into the firm as capital were not provable against the estate of the partnership in bankruptcy. The facts in this case show that the money borrowed was obtained by the individuals for the purpose of contributing each his share to the capital of the partnership. These debts were of the character of the claims of George Stoddard in the present case, based upon the notes of A. K. Stoddard given to George Stoddard for his share in the partnership. It was correctly held by the court, that this was an individual debt, and not provable

against the partnership. But there is a distinction between debts incurred by individuals for the benefit of the individuals in contributing capital to a partnership and debts incurred by a partnership in the business of and for the benefit of the partnership."

68. *Wallerstein v. Ervin*, 7 A. B. R. 256, 112 Fed. 124 (C. C. A. Penn., affirming *In re Ervin*, 6 A. B. R. 356, 109 Fed. 135).

69. *In re Ervin*, 7 A. B. R. 480, 114 Fed. 596 (D. C. Penn.).

69a. Compare *Mayes v. Palmer*, 31 A. B. R. 225, 208 Fed. 97 (C. C. A. Mo.).

70. *Davis v. Turner*, 9 A. B. R. 704, 120 Fed. 605 (C. C. A. N. Car., reversing *In re Jones*, 8 A. B. R. 626, 116 Fed. 341); *In re Stoddard Bros. Lumber Co.*, 22 A. B. R. 435, 169 Fed. 190 (D. C. Idaho, affirmed sub nom. *Mock v. Stoddard*, 24 A. B. R. 403, 177 Fed. 611, C. C. A.);

Thus, parol evidence is admissible to show written obligations signed in the individual names of the several partners nevertheless to be firm obligations,⁷¹ such being held as to notes and a chattel mortgage in the individual names of the partners upon all the firm goods, even where the notes were under seal.

§ 2246. Partnership Released by Creditor's Acceptance of Individual Obligation.—The partnership, on the other hand, may be released from its obligation on a firm debt by the creditor's acceptance of the individual obligation of one of the partners therefor.⁷²

§ 2247. Secret Partner's Claim, Not Debt against Partnership.—A secret partner's claim is not to be allowed as a debt against the partnership.⁷³

§ 2247¹/₄. Nor Is a Partner's Contribution of Capital.—Nor is a partner's contribution to the capital of the firm a provable debt against the partnership assets.⁷⁴

Mock v. Stoddard, 24 A. B. R. 43, 177 Fed. 611 (C. C. A. Idaho, affirming *In re Stoddard Bros. Lumber Co.*, 22 A. B. R. 435, 169 Fed. 190). [1867] *In re Warren*, 2 Ware 322, Fed. Cas. No. 17,191; [1867] *In re Thomas*, 8 Biss. 139, Fed. Cas. No. 13,886.

In re Shattuck & Bugh, 6 A. B. R. 56 (Ref. N. Y.): In this case the court held that claims based on notes signed in individual names of the co-partners, who were the sons of the persons who loaned the money on them and became endorers on other notes, where the payees gave the credit to the firm and not to the individuals, and the proceeds of the notes were used in the business of and for the benefit of the firm, were claims against the partnership.

In re Weisenberg & Co., 12 A. B. R. 418, 131 Fed. 517 (D. C. Ky.): In this case the court held that a claim upon the joint note of two partners could not be allowed against the partnership estate in bankruptcy or on a par with firm creditors: but that parol evidence was admissible to show the liability of the makers of the note to be in fact the liability of the firm.

The presumption that a partner has knowledge of entries in the firm books is rebutted by his uncontradicted testimony that, though he could have had access to the books, he never examined them. *First Nat. Bk. v. State Bk.*, 12 A. B. R. 429, 131 Fed. 422 (C. C. A. Mont., affirming *In re McIntire*, 12 A. B. R. 787, 132 Fed. 265, D. C. Mont.).

But the creditor's testimony, that he intended to give credit to the firm, has been held inadmissible. *In re Weisenberg & Co.*, 12 A. B. R. 418 (D. C. Ky.).

Compare, *In re Lamon*, 22 A. B. R. 635, 171 Fed. 516 (D. C. N. Y.), wherein evidence held not to sustain contention that it was a partnership obligation.

71. *Mock v. Stoddard*, 24 A. B. R. 403, 177 Fed. 611 (C. C. A. Idaho, affirming *In re Stoddard Bros. Lumber Co.*, 22 A. B. R. 435, 169 Fed. 190).

Compare *Adams v. Decker's Lumber Co.*, 29 A. B. R. 42, 202 Fed. 48 (C. C. A. W. Va.).

72. *In re Lehigh Lumber Co.*, 4 A. B. R. 221, 101 Fed. 216 (D. C. Pa.).

73. Instance, *Rush v. Lake*, 10 A. B. R. 455, 122 Fed. 561 (C. C. A. Wash., reversing *In re Clark*, 7 A. B. R. 96, 111 Fed. 893). Inferentially, *In re Stoddard Bros. Lumber Co.*, 22 A. B. R. 435, 169 Fed. 190 (D. C. Idaho).

No Notice Requisite on Retirement of Secret Partner.—*In re Stoddard Bros. Lumber Co.*, 22 A. B. R. 435, 169 Fed. 190 (D. C. Idaho, affirmed sub nom. *Mock v. Stoddard*, 24 A. B. R. 403, 177 Fed. 611, C. C. A. Idaho).

74. *In re Floyd & Co.*, 19 A. B. R. 438, 156 Fed. 206 (D. C. N. Car.); *In re Rice*, 21 A. B. R. 205, 164 Fed. 514 (D. C. Pa.), quoted at § 2260. But his excess of contribution may be proved against the other partner's individual estate. See post, § 2259.

§ 2247½. **Nor Is a Note by One Partner for Buying Out Retiring Partner.**—Nor is a note given by one partner for the purchase price of a retiring partner's share a firm obligation.⁷⁵

SUBDIVISION "B."

PARTNERSHIP DEBTS AND ASSETS IN INDIVIDUAL BANKRUPTCIES IN GENERAL.

§ 2248. **Trustee in Individual Bankruptcy of Partner Not to Interfere with Firm Assets, without Consent.**—A trustee in bankruptcy of an individual partner has no right to interfere with the firm assets [without the consent of the partner not bankrupt].⁷⁶

Moses v. Pond, 4 A. B. R. 655 (N. Y. Sup. Ct.): "There is no view of the scope of the Bankrupt Act which requires the trustee to assume possession of the property of others, or of a partnership, because merely the individual he represents has the ultimate remainder in whatever is left after paying the debts of the partnership, and, possibly, the superior interest of the deceased partner."

In re Pierce, 4 A. B. R. 489, 102 Fed. 977 (D. C. Wash.): "If the administrator (of the deceased partner's estate) will voluntarily surrender possession of the estate, the trustee may take it; but the trustee cannot take possession of any property of which the administrator has custody without his consent."

Obiter, *Mills v. Fisher & Co.*, 20 A. B. R. 237, 159 Fed. 897 (C. C. A. Tenn.): "When there is no adjudication against the firm, the firm assets cannot be administered by the bankrupt court, if there be one member not adjudicated, unless he consent. In such cases the unadjudicated partner has the right to wind up the firm, paying over only the share of the bankrupt partner to his trustee."

§ 2249. **Member Bankrupt, but Partnership Not, Remaining Partners to Account for Bankrupt's Share.**—Where partnership property in which an individual bankrupt has an interest as one of the partners, is not in the custody of the bankrupt's trustee, the bankrupt's interest therein

75. *Mock v. Stoddard*, 24 A. B. R. 403, 177 Fed. 611 (C. C. A. Idaho, affirming *In re Stoddard Bros. Lumber Co.*, 22 A. B. R. 435, 169 Fed. 190), quoted post, § 2263.

76. *Ludowici Tile Roofing Co. v. Penn. Inst.*, 8 A. B. R. 739 (D. C. Pa.); compare, *In re Mercur*, 10 A. B. R. 505, 122 Fed. 384 (C. C. A. Pa.).

It has been held, that a trustee in bankruptcy of a partnership may by summary order in the bankruptcy proceedings obtain surrender of assets in the hands of an assignee or administrator of one of the individual members of the partnership although such member is not himself a bankrupt. *In re Stokes*, 6 A. B. R. 262, 106 Fed. 312 (D. C. Penna.). This decision does not seem to be correct.

Sub-Partnerships.—Where a bankrupt partnership has itself been a partner in another and quite separate partnership enterprise, the same rules would apply—the sub-partnership's affairs are not to be administered in the partnership bankruptcy without the consent of the solvent sub-partner. Instance, but point not raised, *In re Kessler & Co.*, 23 A. B. R. 391, 174 Fed. 906 (D. C. N. Y.), wherein the court held the foreign solvent sub-partner might retain certain shares of sub-partnership stock which had been wholly paid for by the foreign solvent sub-partner.

Lien of Solvent Sub-Partner on Sub-Partnership Assets.—See *In re Kessler & Co.*, 23 A. B. R. 391, 174 Fed. 906 (D. C. N. Y.).

is, in general, to be treated like any other joint interest a bankrupt might have. The only right of the creditor's trustee is to require the persons who hold the remaining interests and have possession of the partnership property, to account for the bankrupt's interest.⁷⁷

§ 2250. In What Court Trustee to Seek Accounting.—The trustee must seek such accounting in the court which would have had jurisdiction had there been no bankruptcy.⁷⁸ And a state court already in possession need not turn over the assets;⁷⁹ save that in case questions of preference or transfers voidable as to creditors are involved, the bankruptcy court, of course, might have jurisdiction in conformity with the usual rules.

But the bankruptcy court will not necessarily attempt to determine the equities of the two partners inter sese, but will remit the solvent partner to a court of equity for a settlement of his claim against the bankrupt co-partner, where the bankrupt co-partner was indebted neither to the firm nor to the solvent partner at the date of adjudication and the solvent partner's claim arose during the process of liquidation, after the adjudication of bankruptcy.⁸⁰

§ 2251. Partnership Affairs Not to Be Administered in Individual Bankruptcy, Except by Consent.—And the partnership affairs are not to be administered by the trustee of the individual bankrupt without the consent of the remaining members.⁸¹

§ 2252. But May Be So Administered if Nonbankrupt Partner Consents.—But partnership assets may be administered in the individual

77. *Deaf & Dumb Institute v. Crockett*, 17 A. B. R. 240 (N. Y. Sup. Ct. App. Div.).

78. Compare, *In re Walker*, 23 A. B. R. 805, 176 Fed. 455 (D. C. Ala.).

79. Inferentially, obiter, *Moses v. Pond*, 4 A. B. R. 655 (N. Y. Sup. Ct.).

80. *In re Walker*, 23 A. B. R. 805, 176 Fed. 455 (D. C. Ala.).

81. Bankr. Act, § 5 (h): "In the event of one or more but not all of the members of a partnership being adjudged bankrupt, the partnership property shall not be administered in bankruptcy, unless by consent of the partner or partners adjudged bankrupt; but such partner or partners not adjudged bankrupt shall settle the partnership business as expeditiously as its nature will permit, and account for the interest of the partner or partners adjudged bankrupt." See ante, § 2248.

In re Pierce, 4 A. B. R. 489, 102 Fed. 977 (D. C. Wash.); *Moses v. Pond*, 4 A. B. R. 655 (Sup. Ct. N. Y.). In-

stance, *In re Walker*, 23 A. B. R. 805, 176 Fed. 455 (D. C. Ala.).

This provision does not apply to cases where the nonconsenting partner is an infant. *In re Dunnigan Bros.*, 2 A. B. R. 628, 95 Fed. 428 (D. C. Mass.). Nor where the nonconsenting partner has sold out to the remaining partner. *In re Denning*, 8 A. B. R. 133, 114 Fed. 219 (D. C. Mass.).

See *In re Blair*, 3 A. B. R. 588, 99 Fed. 76 (D. C. N. Y.), for a curious misunderstanding of this section, the court therein evidently considering that even in partnership cases firm assets may not be administered in bankruptcy except by consent of the partner not adjudged bankrupt.

See *Strause v. Hooper*, 5 A. B. R. 228, 105 Fed. 590 (D. C. N. Car.), for another evident misunderstanding of this section, the court therein considering that it means that in partnership cases the individual estates are not necessarily drawn into the administration of the firm assets.

bankruptcy proceedings of one of the partners, if the other partner or partners consent.⁸²

§ 2253. **"Consent," a Question of Fact.**—When it is that the remaining partners shall be deemed to have given "consent" to the administration of their partnership affairs in the individual bankruptcy proceedings of a bankrupt partner, is a question of fact to be arrived at from a consideration of all the circumstances.

For the remaining partner to stand idly by without protest, when the trustee of his bankrupt partner has assumed administration of the partnership assets, has been held to be such an acquiescence as will amount to a consent to have the partnership affairs administered in the individual bankruptcy.⁸³

The joining by the non-bankrupt partner with a firm creditor in a petition asking that the former firm assets be applied first on firm debts, of course is such consent.⁸⁴

§ 2254. **Partnership Property Comes into Individual Bankruptcy Burdened with Lien in Favor of Firm Creditors.**—Where partnership property comes into the custody of the trustee of the individual estate of one of the partners who is bankrupt, it comes into the custody with a lien upon it in favor of partnership creditors, and the trustee must satisfy them therefrom before individual creditors.⁸⁵

And the trustee of the individual partner may be summarily ordered to surrender the partnership assets to the trustee of the partnership where the partnership is subsequently adjudged bankrupt.⁸⁶

§ 2255. **Individual Creditors Exhaust Individual Property, Firm Creditors, Firm Property—Each Sharing Only in Any Surplus of Other.**—Individual debts should first be paid out of the individual bankrupt's individual estate; partnership debts out of the partnership property, precisely as in cases where a partnership itself is in bankruptcy.⁸⁷

82. In re Harris, 4 A. B. R. 132, 108 Fed. 517 (Ref. Ohio, affirmed by D. C.); In re Pierce, 4 A. B. R. 489, 102 Fed. 977 (D. C. Wash.); In re Filmar (Lippincott v. Klosterman), 24 A. B. R. 194, 177 Fed. 170 (C. C. A. Ill.), quoted at § 2269.

83. In re Harris, 4 A. B. R. 132, 102 Fed. 517 (Ref. Ohio, affirmed by D. C.); compare, analogously, Chem. Nat. Bk. v. Meyer, 1 A. B. R. 565, 98 Fed. 976 (D. C. N. Y., affirmed In re Meyer, 3 A. B. R. 559, 97 Fed. 757).

84. In re Filmar (Lippincott v. Klosterman), 24 A. B. R. 194, 177 Fed. 170 (C. C. A. Ill.), quoted at § 2269.

85. In re Mosier, 7 A. B. R. 268, 112 Fed. 138 (D. C. Vt.); inferentially, In re Head & Smith, 7 A. B. R. 556, 114

Fed. 489 (D. C. Ark.); In re Denning, 8 A. B. R. 136 (D. C. Mass.); impliedly, In re Blanchard, 20 A. B. R. 417, 161 Fed. 793 (D. C. N. Car.); In re Filmar (Lippincott v. Klosterman), 24 A. B. R. 194, 177 Fed. 170 (C. C. A. Ill.), quoted at § 2269. Compare post, § 2269.

86. Manson v. Williams, 18 A. B. R. 674, 153 Fed. 525 (C. C. A. Me.).

87. See ante, § 2238; In re Blanchard, 20 A. B. R. 417, 161 Fed. 793 (D. C. N. Car.); obiter, Mayes v. Palmer, 31 A. B. R. 225, 208 Fed. 97 (C. C. A. Mo.); In re Union Bank, etc., Co., 25 A. B. R. 148, 184 Fed. 224 (C. C. A. Mich.). In re Wilcox, 2 A. B. R. 117, 94 Fed. 84 (D. C. Mass.), cited with approval in In re Daniels, 6 A. B. R.

Euclid Nat'l Bk. v. Union Trust Co., 17 A. B. R. 834 (C. C. A. W. Va., affirming *In re Henderson*, 16 A. B. R. 91, 142 Fed. 588): "The language of subsection 'f' would seem to be too clear to admit of serious doubt as to its meaning, namely, that the estate of the individual bankrupt should be first applied to individual debts, and those of the firm to the firm debts, and that only the surplus of the estate over and above what was necessary to pay the individual debts on the one hand, or the social creditors on the other, could be used and applied alike to the payment and adjustment of the individual and partnership debts, as the case may be. Indeed, the Act plainly limits this latter application of the assets to the surplus thereof, as distinguished from the estate generally."

In re Mills, 2 A. B. R. 667, 95 Fed. 269 (D. C. Ind.): "The general rule in this kind of cases is thus stated by Chancellor Kent: 'The joint creditors have the primary claim upon the joint fund, in the distribution of the assets of bankrupt or insolvent partners, and the partnership debts are to be settled before any division of the funds takes place. So far as the partnership property has been acquired by means of partnership debts, those debts have, in equity, a priority of claim to be discharged; and the separate creditors are only entitled, in equity, to seek payment from the surplus of the joint fund after satisfaction of the joint debts. The equity of the rule, on the other hand, equally requires that the joint creditors should only look to the surplus of the separate estates of the partners after payment of the separate debts.' 3 Kent. Comm. (10th Ed.) p. 78."

To the same effect, *Vaccaro v. Security Bk.*, 4 A. B. R. 482, 103 Fed. 436 (C. C. A. Tenn.): "It is true that in equity the individual debts of a partner are entitled to be first paid out of individual property and firm debts out of partnership property, but in each case the surplus, after providing for the preferred debts, is applicable to the payment of debts of the other class."

Obiter, *Mills v. Fisher & Co.*, 20 A. B. R. 237, 159 Fed. 897 (C. C. A. Tenn.): "In bankruptcy the assets of a bankrupt partnership must be first applied to the payment of partnership debts and the individual assets to the payment of individual debts. The joint creditors are only entitled to share in the surplus of the individual assets and the individual creditors only in the surplus of joint or firm assets."

§ 2256. Even Where No Partnership Assets.—And it makes no difference that there are no partnership assets.⁸⁸

700, 110 Fed. 745 (D. C. N. Y.), and not with disfavor in *Buckingham v. Bank*, 12 A. B. R. 469, 131 Fed. 192 (C. C. A. Tenn.); *In re Henderson*, 16 A. B. R. 91, 128 Fed. 527 (D. C. W. Va.); obiter, *Jacobs v. Van Sickel*, 10 A. B. R. 519, 123 Fed. 340 (D. C. N. J.); *In re Bates*, 4 A. B. R. 263 (D. C. Vt.), quoted ante, § 2237. *In re Corcoran*, 12 A. B. R. 283 (Ref. Ohio, affirmed by D. C.); *Jarecki Mfg. Co. v. McElwaine*, 5 A. B. R. 751, 107 Fed. 249 (C. C. A. Ind.); *In re Wiseman*, 10 A. B. R. 550, 123 Fed. 185 (D. C. affirmed sub nom. *Hibberd v. McGill*, 12 A. B. R. 101).

Hibberd v. McGill, 12 A. B. R. 101, 129 Fed. 590 (C. C. A.): In an individual bankruptcy, a creditor is not

bound by the entry of the partnership books of his claim and payments thereon as a partnership obligation.

Inferentially, *In re Janes*, 13 A. B. R. 341, 133 Fed. 912 (C. C. A. N. Y., reversing *In re Janes*, 11 A. B. R. 792); obiter, *In re Mason & Son*, 2 A. B. R. 64 (Ref. R. I.); obiter, *In re Daniels*, 6 A. B. R. 700, 110 Fed. 745 (D. C. R. I.); *Deaf & Dumb Institute v. Crockett*, 17 A. B. R. 233 (N. Y. Sup. Ct. App. Div.); obiter, *In re Diamond*, 17 A. B. R. 564 (C. C. A. N. Y.).

⁸⁸ *In re Wilcox*, 2 A. B. R. 117, 94 Fed. 84 (D. C. Mass.); *In re Corcoran*, 12 A. B. R. 283 (Ref. Ohio, affirmed by D. C.); inferentially, *In re Janes*, 13 A. B. R. 341, 133 Fed. 912 (C. C. A. N. Y.); obiter, *In re Daniels*, 6 A. B.

Euclid Nat. Bk. v. Union Trust Co., 17 A. B. R. 834 (C. C. A. W. Va., affirming *In re Henderson*, 16 A. B. R. 91): "The contention, however, is earnestly made that notwithstanding the clear and unambiguous provisions of the Act, and the apparent justice thereof, a different rule should be adopted, and an exception made in cases where there is no partnership estate, and that in such a contingency the social creditors have a right to share along *pari passu* with the individual creditors, in the distribution of the latter estate. The question thus raised is not a new one, either under this or the former Bankruptcy Acts, and has given rise to much discussion in this country and England, resulting in many conflicting decisions, and an apparently hopeless confusion of the subject. We are disinclined to enter into a general discussion of the various and irreconcilable opinions found in the reported cases. The decision of Judge Lowell in *In re Wilcox* (D. C.), 2 Am. B. R. 177, 94 Fed. 84, contains an extended review of the entire subject, and especially a history of the law, to which we take the liberty of referring. The Circuit Court of Appeals of two of the circuits have taken antagonistic views of the present Bankruptcy Act. In *Conrader v. Cohen*, 9 A. B. R. 619, 121 Fed. 801, a decision of the Circuit Court of Appeals for the Third Circuit, the petitions' right to share as partnership creditors in the individual assets of the bankrupt is fully recognized; and in *In re Janes*, 13 A. B. R. 341, 133 Fed. 912, a decision of the Circuit Court of Appeals for the Second Circuit, the contrary view is taken. A careful consideration of the entire subject and review of the authorities convinces this court that, whatever may have been the correct rule under former Bankruptcy Acts, the latter case, a decision of Judge Lacombe, of the Second Circuit, concurred in by Judges Wallace and Townsend, presents the correct construction of the law under the present Act; and, however much force there may have been in the contention made by petitioners under the former bankruptcy acts, or what may be the correct general doctrine applicable to the settlement and distribution of partnership estates, that it was clearly within the power of Congress to adopt a method for marshaling such assets, to be applied to the respective classes of creditors, which it has done, and in terms too clear and comprehensive to admit of the necessity for interpretation further than to adopt and follow its plain mandates."

Nor does it make any difference that the partnership funds have been previously exhausted and applied on the same debt outside of bankruptcy.⁸⁹

§ 2257. Even Where No Partnership Assets and All Partners Insolvent.—Where there are no partnership assets and all the partners are dead or insolvent, yet firm creditors are not entitled to share *pari passu* with the individual creditors of the bankrupt in the distribution of his individual estate, but are relegated to the surplus.⁹⁰

R. 700, 110 Fed. 745 (D. C. R. I.); contra, *Conrader v. Cohen*, 9 A. B. R. 619, 121 Fed. 801 (C. C. A. Pa.); contra, *In re Green*, 8 A. B. R. 553, 116 Fed. 118 (D. C. Iowa); contra, *In re Gray et al.*, 31 A. B. R. 146, 208 Fed. 959 (D. C. Pa.).

⁸⁹. *In re Mills*, 2 A. B. R. 667, 95 Fed. 269 (D. C. Ind.).

⁹⁰. *In re Mills*, 2 A. B. R. 667, 95 Fed. 269 (D. C. Ind.); *In re Janes*, 13 A. B. R. 341, 133 Fed. 912 (C. C. A.

N. Y., reversing 11 A. B. R. 792); *Euclid Nat'l Bk. v. Union Trust Co.*, 17 A. B. R. 837 (C. C. A. W. Va., affirming *In re Henderson*, 16 A. B. R. 91, 142 Fed. 568, quoted in preceding section); *In re Corcoran*, 12 A. B. R. 283 (Ref. Ohio, affirmed by D. C.); compare, obiter, *Buckingham v. First Nat'l Bk.*, 12 A. B. R. 465 (C. C. A. Tenn.); contra, obiter, *In re Gerson*, 5 A. B. R. 480 (Ref. Pa.); contra [1867] *In re Downing*, Fed. Cas. 4,044; con-

The leading case upon this point under the present act, containing the history and development of the entire subject is *In re Wilcox*, 2 A. B. R. 117, 94 Fed. 84 (D. C. Mass., cited with approval in *In re Daniels*, 6 A. B. R. 700, 110 Fed. 745, D. C. N. Y., and in *Buckingham v. First Nat'l Bk.*, 12 A. B. R. 469, 131 Fed. 192, C. C. A. Tenn., and in note to *In re Mills*, 2 A. B. R. 668, 95 Fed. 269, but criticised in *In re Greene*, 8 A. B. R. 555, 116 Fed. 118, D. C. Iowa): "To this history of the rule of distribution there should be added some short consideration of the principles upon which the rule is supposed to rest, and these can neither be found nor applied without difficulty. In several cases, and in the writings of many persons learned in the law, elaborate arguments have been made to show that the rule which gives the separate creditor a prior claim on the separate estate is unsound in principle, and works unfairly in not a few instances. Eden, *Bankr. Law* (2d ed.), 169; 2 *Christ. Bankr.* (2d. ed.), 35; Evans' Letter to Sir S. Romilly (1810), p. 81; Story, *Partn.*, § 376. Indeed, some of the arguments used in support of the rule rather make against it. Thus it has been said that the rule is based upon the theory that the joint creditor gives credit to the joint estate, and the separate creditor to the separate estate. The facts are often quite otherwise. A man lending money to a firm lends it upon the credit of the individual estates of the separate partners as well as upon that part of their property which is engaged in the firm business; and, on the other hand, the separate creditor of a partner—his butcher or tailor, for example—gives him credit quite as much upon the successful firm business in which he is supposed to be engaged as upon any property in his separate ownership. It has been said that, inasmuch as the law has laid down the rule of distribution as above stated, creditors know the rule, and give credit accordingly; but this argument, if made in support of the reasonableness of the rule, is vicious by proceeding in a circle. It makes the creditor give credit to a fund because such is the law, and makes the fact that he has given credit to the fund a reason for the law. The rule has been defended upon the ground that it is, in substance, a marshaling of assets; but it goes much further than the marshaling of assets in equity, and the confusion into which this treatment of the rule—as merely a marshaling of assets—brings a court is shown by the opinions in *Lodge v. Pritchard* and other cases. The rule does not carry out the mercantile theory of the partnership relation. Cory, *Accts.* (2d ed.) 124.

"The historical origin of the rules lies not improbably in an ancient practice of distributing the joint estate under a joint commission and the separate estate under a separate commission, each commission dealing with its corresponding creditors. The best theoretic defence of the rule is probably this: The operation of the law of partnership which gives to any separate partner or his assignee only his net share of the partnership assets—a rule manifestly founded in justice and convenience—usually insures to the joint creditors a priority in the application of the joint estate, and therefore this half of the rule has seldom been questioned. The priority given to the separate creditor in the application of the separate estate is a rough, but practical, offset to the inequality caused by the rule governing the application of the

tra, [1867] *In re Jewett*, Fed. Cas. 7,304; contra, [1867] *In re Knight*, Fed. Cas. 7,880; contra, [1867] *In re McEwen*, Fed. Cas. 8,783; contra, [1867] *In re Pease*, Fed. Cas. 10,881; contra, [1867] *In re Slocum*, Fed. Cas. 12,950; contra, [1867] *In re Litchfield*, 5 Fed. 47; contra, [1867] *In re Blumer*, 12

Fed. 489; contra, [1867] *In re Lloyd*, 22 Fed. 88; contra, [1867] *In re West*, 39 Fed. 203; contra, *In re Gray et al.*, 31 A. B. R. 146, 208 Fed. 959 (D. C. Pa.).

As to discharge of firm debts in individual bankruptcies, see post, § 2794.

joint estate. See the dissenting opinion of Judge Gibson in *Bell v. Newman*, 5 Serg. & R. 78. Entirely apart from statute, however, two things are quite clear: First, that the general rule, with some variations, is established in the courts of this country and of England; and, second, that these variations and particularly the exception in the absence of joint estate, have tended to discredit the rule, and to confuse its operations, rather than to obviate its difficulties. * * * The Bankrupt Act of 1800 (2 Stat. 19) contained no reference to the distribution of the assets of a partnership and its component partners, and, except *Tucker v. Oxley*, no decision made under that act has been found which bears upon the question. * * *

"Act 1867, § 36 (Rev. St., § 5121), is, in all essentials, the same as § 14 of the Act of 1841."

In *re Henderson*, 16 A. B. R. 91, 128 Fed. 527 (D. C. W. Va., affirmed sub nom. *Euclid Nat'l Bk. v. Union Trust Co.*, 17 A. B. R. 837 (C. C. A. W. Va.): " * * * after long and careful consideration, that judgment is that the exception is not warranted. I reach this conclusion for these, among other, reasons. First. It is admitted to be an exception to a general rule, which rule is plain, clear, apt, and in unambiguous language is written in the law itself, while the exception is not; on the contrary, it must depend solely upon judicial construction, which because it in effect provides a different method of distribution from that provided by the law itself, can not be considered short of mere judicial legislation. It is to be recalled how easily the Congress, had it designed such exception to be made, could have incorporated it as such in the law itself. It can not for a moment be presumed that the matter was overlooked. On the contrary, it is to be remembered that this Bankruptcy Act was as carefully considered a piece of legislation as any given us for years by that body. The Senate first passed what was known as the 'Nelson' bill on the subject. The House of Representatives, after long discussion, passed, as a substitute, the 'Henderson' bill carrying out substantially the provisions of the Torrey measure, which had been for several years prior discussed in legal associations and journals. The matter was finally referred to a conference committee composed of Senators Hoar, Lindsay, and Nelson on behalf of the Senate, and Representatives Henderson, Ray (now judge of the Northern district of New York) and Terry on behalf of the House, lawyers as able as the country could afford, who, after several months' deliberation, reported a compromise which was passed without amendment and became the existing Act. The fact that the courts had established such exception in the construction of the Act of 1867, but with conflict of opinion, is one of the strongest reasons in convincing me that Congress never intended to recognize such exception, for knowing of the former conflict of opinion, and of the action of the courts under the former act in establishing it, instead of recognizing it, which could have been done in a few lines, it does not do so, but, in plainer, more simple, positive, and direct language, reiterates the rule, without exception or qualification, that partnership assets shall pay partnership debts, individual assets individual debts, and only surpluses shall be applied, the one to the other. The argument made that such exception is in accord, generally, with the law and practice in the States, only strengthens my view as to the purpose and intention of the Congress. Its members, coming from all the States and having full knowledge of such practice and law, would seem to have deliberately purposed that this uniform bankrupt act, which was to be the supreme law of the land, should not recognize such exception but, in effect, exclude it.

"Second. Nor can I read paragraph 'g' as giving any excuse for the establishment of such exception by judicial construction. Clause 'f' states the

precepts of the law; clause 'g' relates to the procedure under it. The law in 'f' demands that 'the net proceeds shall be appropriated' as directed by it, while 'g' provides simply that in carrying out these precepts, and as an aid in doing so, the court may do certain things, to wit, permit proof of claims of partnership estates against individual estates, and vice versa, and marshal the assets of such estates so as to prevent preferences and secure equitable distribution of such estates. Note the use in this paragraph of the word 'estate' instead of the word 'debt' as used elsewhere. It is properly used and was designed to meet such cases as, for example, where the partnership estate might have a just claim against one of its individual members who had not paid into the partnership his full share of any part of the capital which he was legally bound to do, while the other members of the partnership perhaps had done so; or, vice versa, where the individual member, a bankrupt, had paid into the partnership fund all of his pledged capital, while the other members had not. To meet such and other similar cases that might arise, I am convinced, was the sole cause and scope of this permissive clause in procedure, only mandatory in cases where the circumstances, in equity and good conscience, required its application. The necessity for this permissive provision in procedure is the more apparent when we read in clause 'h' that where all members of a partnership are not adjudged bankrupt, the partnership property is not to be administered in bankruptcy without consent of the solvent partners, a provision not in our former bankrupt laws. In such case, without this clause 'g', would the bankrupt court have jurisdiction to determine any such questions as referred to above between two estates that might arise in the adjustment of their respective rights; the one being administered by the court, the other by the solvent partners?

"Finally, I do not believe any just criticism can be made of the legislative body for establishing this rule and refusing to incorporate the exception contended for to it, into the law. Judge Lowell in *re Wilcox*, *supra*, has shown how much difficulty, perplexity, and conflict have arisen during more than three centuries, in the settlement of these joint and separate estates. Under such circumstances, Congress could well say that it was time, in this law which was to be supreme and uniform throughout the States, to settle the vexed controversy by a direct and positive, if arbitrary, rule. It is true in regard to all such rules that, under exceptional circumstances, they work hardships, but the ultimate good they accomplish largely counterbalances the evil. Who doubts longer the benefits of statutes of limitation?

"The rule established here has the merit of simplicity and directness. It gives full and complete repose, and I submit it is as nearly equitable as any such rules can be. Under modern business conditions, a man can become partner in an unlimited number of partnerships of which, and of his connection therewith, his neighbor, who is trusting him upon faith of his individual merit and financial worth, can know nothing, and these partnerships with or without his knowledge may be, by bad or extravagant management, accumulating debt against him many times over the total value of his estate. These partnerships may be located in different localities far separate. For instance, he may be a partner in a 'Eureka Gold Mining Company,' in Alaska, an 'Excelsior Construction Company' in New York, a 'Superlative Fruit Company' in Florida—no one of which in name may disclose his connection therewith. Why is it not reasonable to protect, under such conditions, his neighbors at home who have trusted him, as against the creditors of these distant partnerships, who have in most cases credited such partnerships upon faith of the business they were doing and without knowledge of him or of his connection therewith, until their

bankruptcy occurs? Is there not a plain dividing line based on reason and sound equity? His neighbors trusted him with his personal property before them; the others trusted the partnership with its property in view. Why should not each class resort to the property that was the basis of their respective extensions of credit, without the one having any advantage over the other, and what matters it if the creditors of the partnership have been so foolish as to extend credit to it when it has no property, any more than where a man's neighbor has been just as foolish in extending credit to him personally when he had none? Has it ever been contended, in a case where a man has taken his personal property and invested it in a partnership so that he has nothing, that an exception should be judiciously created which would permit his individual creditors, in a bankruptcy proceedings against the partnership, to come in and share *pari passu* with the partnership creditors, as against his interest therein? Why is not one proposition as fair as the other in good conscience, and why does not the simple rule established by Congress settle the question as fairly as it can be settled? Whether it does or not, of the one thing I am entirely satisfied; and that is, that the rule itself can not justly be more severely criticised than can be the 'exception' contended for. This exception certainly is none the less arbitrary, and leads to no less absurd results. This was recognized by the courts creating it in construing the law of 1867. For example, *In re Blumer* (D. C.), 12 Fed. 489, from the Eastern District of Pennsylvania, it was held:

"If, after deducting the portion of costs chargeable to the partnership estate, there is any balance of partnership assets, however small, the partnership creditor will not be entitled to share *pari passu* with the separate creditors in the distribution of the separate estate.'

"In other words, the application of this exception might well turn on the partnership possession of, say, 30 cents. Again, *In re Marwick*, Fed. Cas. No. 9,181, it is held:

"If there be any joint fund, however small, such proof cannot be allowed, although such fund may have been created by the separate creditors purchasing some of the partnership assets, actually worthless, for the purpose only of creating it; for if there be a joint fund, the court cannot, under the statute, look behind the fact, to inquire how it has been produced.'

"In other words, under the operation of this exception, a contribution of a few cents, no matter by whom, to the partnership assets, would wholly prevent its application."

Obiter, *In re Daniels*, 6 A. B. R. 700, 110 Fed. 745 (D. C. R. I.): "Where a member of a copartnership is adjudged a bankrupt in his individual capacity, creditors of the firm are not entitled to receive dividends out of his individual estate until his individual creditors have been paid in full; and this rule prevails notwithstanding the fact that there are no firm assets."

Contra, *Conrader v. Cohen*, 9 A. B. R. 619, 121 Fed. 801 (C. C. A. Penna., affirming *In re Conrader*, 9 A. B. R. 85, 118 Fed. 676): "It will be perceived that a single fund only—derived from the separate estate of the bankrupt, Conrader—was before the court for distribution; that all the property of the firm of Jenkins & Conrader had been sold upon execution in the year 1895 and passed to the sheriff's vendee, that the partnership is not in bankruptcy; that there are no firm assets and that there is no solvent partner. The insolvency of Jenkins in 1895, having been shown, that condition will be presumed to have continued in the absence of any evidence to the contrary. If his financial condition changed it was for the contesting individual to show it. Upon the facts here appearing why should not the firm creditors participate in the fund before the court? It is the only fund available to any of the creditors. Now it

is well settled that each partner is a debtor to the creditors of the firm. In equity, as at law, partnership debts are treated as several as well as joint. Upon principle, we think the District Court was right in admitting the partnership creditors to participate pro rata with the individual creditors in this fund.

"We find abundant authority to sustain the decision of the court below. In *United States v. Lewis*, 13 Nat. Bank Reg. 33, Fed. Cas. No. 8429, held by Mr. Justice Strong and Circuit Judge McKennan, that the rule that the joint estate must be applied to pay joint debts and the separate estate to pay the separate debts, is only applicable where the joint estate, as well as the separate estate to pay the separate debts, is before the court for distribution; and in the same case upon appeal, 92 U. S. 618, 623, the Supreme Court, speaking by Mr. Justice Swayne, said: 'A court of equity will not entertain the question of marshaling assets unless both funds are within the jurisdiction and control of the court.' In the case in hand two funds do not exist. The established English doctrine is thus stated in *Lind. Partners.* (3d Amer. Ed.), p. 731; (6th Ed.), § 749: 'If in the case of a bankrupt firm there is no joint estate, the joint creditors are entitled to rank as separate creditors against the separate estates of the individual partners. So, if one partner only is bankrupt, the creditors of the firm are entitled to rank as separate creditors against the separate estate of the bankrupt, if there is no joint estate and if there is no solvent ostensible partner, at all events none in this country.' The like doctrine is set forth in *Story on Partnership*, § 380, that where there is no partnership assets and no solvent partner, the firm creditors share in the separate estate of the bankrupt partner *pari passu* with the individual creditors was the recognized rule under the Bankrupt Act of 1867."

Also, *contra*, *In re Green*, 8 A. B. R. 553, 116 Fed. 118 (D. C. Iowa): "In support of the ruling made, the referee cites the case of *In re Wilcox*, 2 Am. B. R. 117, 94 Fed. 84, wherein will be found a learned discussion of the general proposition by Judge Lowell, who reaches the conclusion that the partnership creditors cannot be allowed to share with the individual creditors in the assets of one member of the firm, even though there are no firm assets and no proceedings against the firm. If I correctly understand the ruling in this case, it is, in effect, that § 5 of the Bankrupt Act is not to be limited to cases wherein the proceedings are against the firm as well as the individual members, but that it is to be construed to establish the broad principle that the individual creditors of the bankrupt are to be paid in full out of his assets before the claims owing by him as a member of the firm can be allowed to share in his assets, even though the firm had long since been dissolved, and there are no firm assets to be applied to the payment of the firm debts. This question was involved in the case of *In re Keller* (D. C.), 6 Am. B. R. 337, 109 Fed. 118, wherein this court held that as there had been a valid transfer of the partnership property to one of the partners, Almon D. Keller, who subsequently went into bankruptcy as an individual, and transferred to his trustee all of his property, including that which had formerly belonged to the partnership, the firm creditors would be permitted to share equally with the individual creditors in the assets of the estate. This conclusion was based largely upon the fact that the Supreme Court in *Fitzpatrick v. Flannagan*, 106 U. S. 648, 1 Sup. Ct. 369, 27 L. Ed. 211, had declared the equitable rule to be as follows:

"The legal right of a partnership creditor to subject the partnership property to the payment of his debts consists simply in the right to reduce his claim to judgment and to sell the goods of his debtor on execution. His right to appropriate the partnership property specifically to the payment of his

debt in equity, in preference to creditors of an individual partner, is derived through the other partner, whose original right it is to have the partnership assets applied to the payment of partnership obligations. And this equity of the creditor subsists so long as that of the partner, through which it is derived, remains; that is, so long as the partner himself "retains an interest in the firm assets, as a partner, a court of equity will allow the creditors of the firm to avail themselves of his equity, and enforce through it the application of those assets primarily to payment of the debts due them, whenever the property comes under its administration." Such was the language of this court in *Case v. Beauregard*, 99 U. S. 119, 25 L. Ed. 370, in which Mr. Justice Strong, delivering the opinion, continued as follows: "It is indispensable, however, in such relief, when the creditors are, as in the present case, simply contract creditors, that the partnership property should be within the control of the court, and in the course of administration, brought there by the bankruptcy of the firm, or by an assignment, or by the creation of a trust in some mode. This is because neither the partners nor the joint creditors have any specific lien, nor is there any trust that can be enforced, until the property has passed in custodia legis." Hence it follows that "if, before the interposition of the court is asked, the property has ceased to belong to the partnership, if by a bona fide transfer it has become the several property of one partner or of a third person, the equities of the partners are extinguished, and consequently the derivative equities of the creditors are at an end."

"In view of this authoritative declaration that the equities of the partnership creditors are derived from the equity of the partners, and that it is within the power of the partners to put an end to the equities of the firm creditors, by a bona fide transfer of the firm assets to one partner or to a third party, wherein the equity in the ruling that, in cases wherein the equity of the firm creditors has been terminated, not through their act nor with their consent, but by the act of the partners in selling the firm assets to one of their number or to a third party, and subsequently members of the firm are put into bankruptcy as individuals, the individual creditors are entitled to exclude the firm creditors from sharing in the assets until the individual debts are paid in full? In such cases there is no other fund to which the firm creditors can resort for payment, and the practical result of the rule laid down in the *Wilcox* case is that, in all cases wherein the equity of the firm creditors have been destroyed by the action of the partners, in converting the firm property into individual assets by a sale thereof to one of the parties, the individual creditors are entitled to be preferred, and are entitled to exclude the firm creditors from sharing in these assets, even though they were originally the property of the firm. A very large proportion of the cases brought in bankruptcy under the provisions of the present act are cases wherein the bankrupts have been members of one or more partnerships which have been dissolved long since, and in which the only assets are those belonging to the individual bankrupt; and, if it be the rule that the individual creditor is always entitled to be first paid from the individual assets, it follows that in all these cases the debts due the firm creditors are discharged, yet these creditors are barred from any share in the assets of the bankrupt.

"The variant views set forth in the numerous decisions cited in the *Wilcox* case serve to show that it is practically impossible to formulate a single general rule that will meet the equities of every case, but the adoption of the rule that in every instance wherein there are firm and individual creditors, but the assets are individual only, the latter class of creditors are to be paid in full to the exclusion of the firm creditors, will certainly work injustice in so many cases that I

should hesitate long before accepting it in the absence of a controlling decision by an appellate court. The Supreme Court having decided that the firm assets may be converted into individual assets by the action of the partners, I cannot see the equity in the view that holds, in effect, that it is within the power of the partners to determine the equity of the firm creditors in the firm assets, and that the same act which terminates the equity of the firm creditors creates a preference in favor of the individual creditors, enabling them to secure payment in full of their claims out of funds which in many cases are wholly or largely the proceeds of the property which was originally firm assets."

§ 2258. Joint and Several Obligations for Partnership Debt. Share in Individual Estate.—Creditors holding joint and several obligations of the partners for a partnership debt may share in the individual estates of the several partners on an equality with exclusively individual creditors.⁹¹

Buckingham Trustee v. First Nat'l Bk., 12 A. B. R. 465, 131 Fed. 192 (C. C. A. Tenn.): "The next question is whether the claimants * * * as individual creditors of Estes, should be paid out of his individual estate, in preference to the claims of the firm creditors. Doubtless the notes executed by the firm and endorsed by Estes, were firm debts, as well as individual debts of Estes. But the holders had a right, if they preferred, to present them as claims against Estes individually. * * * Gartenlaub was advised of the fact that Estes individually owned a large amount of real estate and for that reason required his individual endorsement."

Inferentially, analogously, *In re McCallum & McCallum*, 11 A. B. R. 448, 127 Fed. 768 (D. C. Pa.): "The facts are these: The bankrupt firm made a promissory note payable to the order of William H. McCallum, one of the partners, by whom it was duly indorsed. The claim against the firm, based upon their contract as makers, was proved by the creditor, but the claim against William's individual estate, based upon the separate and distinct contract of indorsement, has not been proved. The year has gone by, and to permit the proof of claim that is now upon file with the referee to be so amended as to include the second contract would not, in my opinion, be the allowance of an amendment at all, but the allowance of a wholly new claim, in the face of the statutory prohibition. The contract entered into by the maker of a promissory note, and the contract entered into by the indorser are entirely distinct and separate undertakings. It does not affect this conclusion that the contract of indorsement is made by a member of the firm that has previously made the other contract. The same man has made two contracts in different characters, one as a partner and the other as an individual."

[1867] *In re Thomas*, 8 Biss. 139, Fed. Cas. No. 13,886: "There is a class of cases in which it has been held that where a creditor holds notes signed by a firm, and signed or indorsed also by an individual member of the firm, he may prove against both estates, and receive dividends from both. *In re Farnum*, Fed. Cas. No. 4,674; *Mead v. National Bank of Fayetteville*, Fed. Cas. No. 9,366; *Emery v. Canal National Bank*, Fed. Cas. No. 4,446. These cases establish a rule opposed to the old rule on the subject in England, and the

91. *In re McCoy*, 17 A. B. R. 760, 150 Fed. 106 (C. C. A. Ind.); [1867] *Emery v. Canal Nat'l Bk.*, Fed. Cas. 4,446; [1867] *In re Bradley*, Fed. Cas. 1,772; [1867] *In re Farnum*, Fed. Cas. 4,674; [1867] *Mead v. Nat'l Bk.*, 6 Blatchf. 180, Fed. Cas. 9,366; [1867] *In re Bigelow*, 3 Ben. 146 Fed. Cas. 1,397; *In re Terens*, 23 A. B. R. 680, 175 Fed. 495 (D. C. Wis.).

principle thus settled seems to reach out to the question involved in the case at bar. The scope of these decisions is, that when an individual member of a firm, as such, becomes surety upon or indorses an obligation of the firm, he thereby gives what is in the nature of security upon his separate estate to the firm creditors, and, by reason of the individual liability superadded to the joint obligation, he places the firm creditor in a position where he can go against the individual as well as the joint estate. Thus it results, that without the indorsement or individual signature of one of the firm, the firm creditor would have no right to claim against the individual assets until individual creditors had been first satisfied. But holding the individual indorsement or signature, the firm creditor may, in the first instance, prove against the separate as well as the joint estate. Now, such separate liability would seem to be, at least, in the nature of security though differing radically, it is true, in character and form from that of a mortgage, and yet double proof, by the firm creditor in such case, may be made without any abatement of advantage which his diligence has secured."

Contra, *In re Mosier*, 7 A. B. R. 268 (D. C. Vt.): "The joint and several notes given by the partners for partnership liabilities are none the less partnership debts because the partners are also individually liable. By the terms of the same section of the Bankrupt Act, no part of the separate property is to go for partnership debts till the separate debts are fully paid. Therefore there can be no individual assets of Mosier in which these partnership creditors can be entitled to participate.

"Participation of joint and several partnership creditors in individual assets, before individual creditors are paid in full, denied."

Apparently contra, *Bank v. Stevens Estate*, 6 A. B. R. 164, 107 Fed. 245 (D. C. Vt.): "As to the first note the claim is sought to be made individual through the separate indorsement of C. P. Stevens. But it was primarily a partnership note, and, so far as is in any wise made to appear, a partnership debt; and, if Stevens' liability as indorser had been fixed, it would still be apparently a partnership debt. There is no suggestion in the claim that his liability in this respect in any way became fixed, and a fortiori the debt remained a partnership debt without becoming an individual debt."

Thus, misappropriations by a partnership may result in provable claims both against the firm and also against the guilty partners individually.⁹²

In re Coe, 26 A. B. R. 353, 183 Fed. 745 (C. C. A. N. Y., affirming 22 A. B. R. 384, 169 Fed. 1002): "It makes no difference that the partners acted without evil intent, nor that the firm got the benefit of what they did. It remains a wrongful conversion for which all the partners are liable, not jointly as partners, but jointly and severally as tort-feasors, whether they each actively participated in it or not; the acts of every one being imputed to every other. * * * The bank could prove two claims, one against the firm—i. e., the partners jointly on the acceptances—and the other against the partners jointly and severally upon an implied contract (the tort being waived) to repay moneys of the bank wrongfully converted by them. The doctrine of election between inconsistent remedies on the same claim has no application."

⁹² *In re Coe*, 22 A. B. R. 384, 169 Fed. 1002 (D. C. N. Y.), quoted at § 2349; *In re Coe*, 26 A. B. R. 352, 183 Fed. 745 (C. C. A. N. Y.); (1867) *In*

re Baxter, 8 Nat. Bankr. Reg. 62; (1867) *In re Blackford*, 35 App. Div. 330, 54 N. Y. Supp. 972; (Eng.) *Re Parkers*, 19 Q. B. Div. 84.

And a composition effected by the partnership alone will not affect the claims against the individual estate;⁹³ except, of course, to the extent of the amount applied upon the claim by the composition.

Except, of course, to the extent of the amount applied upon the claim by the composition.

A contrary doctrine to that enunciated at the beginning of this section would destroy the advantage to which the creditor is entitled by virtue of the individual signatures.

But a modification of the doctrine has been made in one case where it has been held that such individual proof should be only for the balance left after deduction of the dividends received from the partnership assets.⁹⁴ But such modification seems unwarranted. The least that can be said of the individual obligations is that they are those of sureties. If they are those of sureties then, assuredly, the creditor may prove for the full amount against both the principal and surety's respective estates, so long as the aggregate dividends do not exceed the amount of the claim, applying the dividends first from the principal's estate. Exhausting the principal's dividends first, however, is different from making proof only for the balance after such application.⁹⁵

On the same theory, where the partners and the firm have misappropriated property left with them as bailees, the owner may prove against both the partnership estate and the estate of each partner who participated in the wrong.⁹⁶

§ 2259. Partner's Right of Contribution for Paying Firm Debts, Provable in Other Partner's Bankruptcy.—The right of one partner to contribution from the other partner for paying firm debts is a provable claim against the individual partner in individual bankruptcy.⁹⁷

However, it has been held that the claim of a solvent partner who is liquidating the partnership affairs instead of having them administered in bankruptcy, is not a provable debt against the bankrupt partner where the bankrupt partner was not indebted to the firm nor to the solvent partner at the time of adjudication, the solvent partner's claim arising from subsequent events.⁹⁸

93. In re Coe, 22 A. B. R. 384, 169 Fed. 1002 (D. C. N. Y.), quoted at § 2349.

94. In re McCoy, 17 A. B. R. 760, 150 Fed. 106 (C. C. A. Ind.).

95. See ante, § 758: "No deduction for property of principal held by creditor, where surety bankrupt."

96. In re Coe, 22 A. B. R. 384, 169 Fed. 1002 (D. C. N. Y.); In re Coe, 26 A. B. R. 352, 183 Fed. 745 (C. C. A. N. Y.). Also that a composition effected by the partnership alone would not prevent proof of the debt against the estate of the individual partner, *Ibid*.

97. In re Carmichael, 2 A. B. R. 815, 96 Fed. 594 (D. C. Iowa); In re Stevens, 5 A. B. R. 9, 104 Fed. 323 (D. C. Vt.). Compare, In re Dillon, 4 A. B. R. 63, 100 Fed. 627 (D. C. Mass.). In re Hirth, 26 A. B. R. 666, 189 Fed. 926 (D. C. Minn.); In re Pangborn, 26 A. B. R. 40, 185 Fed. 673 (D. C. Mich.). Compare, *obiter*, *Mock v. Stoddard*, 24 A. B. R. 403, 177 Fed. 611 (C. C. A. Idaho, affirming *In re Stoddard Bros. Lumber Co.*, 22 A. B. R. 435, 169 Fed. 190.). Compare, also, ante, § 2247½.

98. Compare, analogous doctrine, ante, §§ 640, 645, 709, 711.

In *re Walker*, 23 A. B. R. 805, 176 Fed. 455 (D. C. Ala.): "The certificate shows an admission by the parties that at the time of the filing of the petition there was no indebtedness existing upon a partnership settlement, as between the partners, and that the partnership assets, without resort to the individual property of either partner, were amply sufficient to fully pay all the partnership debts. At the time of the filing of the petition in bankruptcy, the bankrupt partner owed the solvent partner nothing, either because of greater contribution to the firm assets by the solvent partner or larger withdrawals therefrom by the bankrupt partner, or because, in order to pay the firm indebtedness, recourse would be necessary upon the solvent partner or his property, after exhaustion of the firm assets. * * * The case is, therefore, not one of an unascertained or unliquidated indebtedness due the solvent partner, Peter Pappas, but one in which there was no indebtedness at all due him at that time from his bankrupt partner. The indebtedness claimed by him arose subsequent to the filing of the petition in bankruptcy, by reason of the solvent partner having elected to take the administration of the partnership assets, which, when the petition was filed, were admittedly ample to pay all partnership debts, but which, owing to subsequently arising causes, failed to realize enough to do so, and by reason of his having undertaken with them to satisfy all the firm debts. If any claim arose in favor of the solvent partner against his copartner because of the insufficiency of the partnership assets to liquidate partnership debts and the consequent necessary resort to the property of the solvent partner for that purpose, it was of subsequent origin to the filing of the petition in bankruptcy, and is not a provable claim against the bankrupt partner, nor one from which a discharge in bankruptcy would release him."

§ 2260. On Marshaling Partnership and Individual Estates, Solvent Partner's Excess Contribution Provable against Individual Estate.—Thus, also, in the marshaling of partnership and individual estates in bankruptcy, a solvent partner's excess of contribution to pay firm debts constitutes a provable debt against the individual estates of the other partners, and may share *pari passu* with individual debts.⁹⁹

But it may not share in partnership assets until partnership creditors are paid.

In *re Rice*, 21 A. B. R. 205, 164 Fed. 514 (D. C. Pa.): "The referee's decision is attacked on the ground that the claim of Joseph A. Rice against the firm is an asset of his individual estate, which belongs to his individual creditors and should not be withheld from them and thus applied in effect to the claims of other partnership creditors than himself. But this argument fails to state the situation precisely. No doubt the claim of Joseph A. Rice against the firm of which he was a member is an asset of his individual estate, but it is an asset with a particular disability, and in this respect it differs from the claims of other partnership creditors. Its disability consists in the fact that, according to the well-settled rule governing the marshaling of partnership and of individual assets, it cannot participate in the distribution of the partnership assets until other partnership creditors have been satisfied in full. For this reason the individual creditors of the claimant cannot profit by it as completely as if he were an ordinary creditor of the firm and not a member also.

99. In *re Stevens*, 5 A. B. R. 9, 105 Fed. 323 (D. C. Vt.).

But nothing is taken away from the individual creditors to which they are equitably entitled, because the claimant himself could not share in the distribution of the partnership assets *pari passu* with other partnership creditors. To sustain the claimant's position would give to his individual creditors a more extensive right against the bankrupt firm than he himself possesses and would thus do violence to the rule that the individual creditors succeed only to such equity in the firm assets as belongs to their debtor himself."

§ 2261. Likewise, Partner's Right of Indemnity (Where Surety) for Paying Copartner's Individual Debt Provable against Copartner's Individual Estate, Entitling to Subrogation to Creditor's Claim.—Thus, where one partner has paid the individual debt of another partner for whom he was surety, his claim for indemnity from his principal is a provable claim against the co-partner's individual estate, and entitles his trustee in bankruptcy to be subrogated to the original creditor's claim, and to prove it against the other partner's individual estate.¹

[1867] In *re May*, Fed. Cas. 9,327: "Partners and their estates come under the rule, for the reason that, in bankruptcy, estates are settled separately; the joint creditors are to have the joint estates, and vice versa, and although there is no contribution between joint and separate estates, unless there should be a surplus of one over the other, yet when the property of one is pledged for the debt of the other, a court of equity will apply the right of subrogation precisely as it would if the contracting parties were not partners, and thus do justice to the different creditors."

§ 2262. But Claim of Retiring Partner for Unpaid Purchase Price of Partnership Share, Not to Share with Partnership Creditors in Surplus of Remaining Partner's Individual Estate.—But the claim of the retiring partner for the purchase price of the latter's share is not to participate *pari passu* with partnership creditors in the individual estate of the remaining partner.² This is so, for the reason that the sale itself, being simply a sale of an undivided interest in the surplus, contemplates satisfaction, first, of all firm obligations in the ascertainment of such surplus.

§ 2262¼. Claim of Bankrupt Partnership against Its Bankrupt Member—Not to Share *Pari Passu* with Individual Creditors.—The doctrine that a partnership is a distinct entity will not be construed to change the established rule fixing the substantive rights of creditors respectively, of the partnership and of its individual members, in order to allow a partnership claim against one of the members to share *pari passu* with the claims of the individual creditors. Whilst the trustee of a bankrupt partnership is entitled to prove its claim against the individual estate

1. In *re Mason & Son*, 2 A. B. R. 60 (Ref. R. I.); [1867] In *re Foote*, Fed. Cas. 4,906.

2. In *re Denning*, 8 A. B. R. 133, 114 Fed. 219 (D. C. Mass.); In *re Gerson*, 5 A. B. R. 480 (Ref. Pa.). Compare, ante, § 2247½.

of a bankrupt member, he is only entitled to share out of the surplus after the other individual creditors are paid in full.

Thus, where both the partnership and the partners individually are bankrupt, the trustee may prove against the separate estate of a partner a debt due the partnership for money loaned by the firm to him, and for which he gave his individual note, but will not be allowed to share *pari passu* with the individual creditors of the bankrupt.

In *re Union Bank, Whitney, et al.*, 25 A. B. R. 148, 158, 184 Fed. 224 (C. A. Mich.): "No objection is made to the proof of the partnership claim nor to a transfer to the partnership assets of any surplus that may remain of Gilkey's individual estate after the claims of his separate creditors are satisfied. The objection is to the alleged right of the partnership through its trustee to share *pro rata* in that estate. Proof but not sharing is mentioned in 5g. To permit sharing upon proof allowed under that paragraph is to ignore most important relations attending a partnership, where, as here, the partnership and its members are alike insolvent and adjudged bankrupts. Neither the bankrupt partnership nor its trustee can have any possible interest in the separate estate of any of the bankrupt partners, except only for the benefit of the partnership creditors. Whatever disability then that can be predicated of the partnership creditors respecting the separate estate and creditors of one of the partners, ought to attach to the bankrupt partnership estate and its trustee. Can it be that in a case like this there is anything in the bankruptcy provisions we have been considering, which requires a court to decline to see or to consider these plain facts? It was long ago settled that the partnership creditors would not either directly or through the assignee be allowed so to deplete the separate estate of one of the partners to the prejudice of his separate creditors (Story on Part., § 391; Gow on Part., Marg. pp. 317, 318; also decisions first cited in this opinion). It is not claimed that this rule of protecting separate creditors should be ignored upon any theory of fraud; for admittedly the claim in question is founded on consent on simple contract. Hence, unless the trustee of the bankrupt partnership is to be accorded greater rights than would be given to those in whose interest alone the claim is pressed, there is nothing to warrant the removal of the separate estate in question from the ordinary category and liabilities of such estates (Story on Part., § 391, note); in short, the partnership estate should not be now any more than it would have been prior to the enactment of the present Bankruptcy Act, allowed to claim against "the separate estate in competition with the separate creditors." *Amsinck v. Bean*, 22 Wall. 395, 402.

§ 2262½. **Vice Versa—Claim of Individual Bankrupt Estate against Firm Estate.**—By § 5 (g) of the Bankrupt Act, "the court may permit the proof of the claim of the partnership estate against the individual estates, and vice versa," hence the trustee of a bankrupt member may prove a debt due the member by the partnership against the estate of the bankrupt partnership, but the claim will only be "formally" allowed, with the qualification that it should not be permitted to share in the distribution of the assets until such partnership creditors as are not members of the firm have been paid in full.³

3. In *re Rice*, 21 A. B. R. 205, 164 Fed. 509 (D. C. Pa.).

In *re Effinger*, 25 A. B. R. 930, 932: "The claim of a partner for money lent to the partnership in excess of the amount he was bound to contribute as his share of the capital is unquestionably provable against the partnership estate, but it cannot share in the distribution of that estate until all the firm creditors are paid. In the third or supplementary volume of Remington, at page 669, § 2247¼, the learned author says: 'Nor is a partner's contribution to the capital of the firm a provable debt against the partnership assets. * * * But his excess contribution may be proved against the other partner's individual estate.'

"We shall see that the cases hold that § 5g authorizing the proof of such claims does not intend to change the previously existing law as to the priority of right to share in the distribution of assets. It is not true, as is contended by the counsel for the individual creditor in this case, that such a construction deprives clause 5g of all significance. In point of fact its enactment abolished a technical rule of bankruptcy procedure which in the past had at times worked real injustice. * * *

"Under our present law claims cannot be proved subsequent to one year after adjudication. Except for § 5g, it would be impossible to prove claims of the partnership estate against the individual estates, or vice versa, until the individual or the firm debts, as the case may be, had been paid in full. Before this could take place, the time in which the claims could be filed would usually have expired."

§ 2262¾. Exception to the Rule That Claim of Bankrupt Partnership against Its Bankrupt Member Not to Share *Pari Passu* with Individual Creditors and Vice Versa.—However, it would appear from some cases that the rule set out in the preceding sections perhaps should be qualified by an exception where the debt due the firm from the individual member is based on fraud,⁴ conversion, etc.; and perhaps, also, where the firm and the individual partner had carried on distinct trades, and the debt is a trade debt resulting from the trade dealings between the partner as a separate trader and his firm. In such cases, it would appear from such rulings that the court in administering the estates would not only permit the "proof" of such claims, but would also allow them to share equally with the individual creditors, or the firm creditors, as the case may be, in order to "secure the equitable distribution of the property of the several estates."

§ 2263. Obligation Signed in Individual Names of Partners, *Prima Facie* Individual Debt.—An obligation signed in the individual names of the partners is *prima facie* their respective individual obligation,⁵ but may be shown by parol evidence to be a firm debt.⁶

Mock v. Stoddard, 24 A. B. R. 403, 177 Fed. 611 (C. C. A. Idaho, affirming In

4. Inferentially, In *re Union Bank, Whitney, et al.*, 25 A. B. R. 148, 184 Fed. 224 (C. C. A. Mich.).

5. In *re Weisenberg & Co.*, 12 A. B. R. 417 (D. C. Ky.); Instance, In *re T. A. McIntyre & Co.*, 28 A. B. R. 459, 198 Fed. 579 (D. C. N. Y.).

6. See converse of rule, ante, § 2240. In *re Stoddard Bros. Lumber Co.*, 22 A. B. R. 435, 169 Fed. 190 (D. C. Idaho), affirmed sub nom. *Mock v. Stoddard*, 24 A. B. R. 403, 177 Fed. 611 (C. C. A.); *Adams v. Lumber Co.*, 29 A. B. R. 42, 202 Fed. 48 (C. C. A. W. Va.).

re Stoddard Bros. Lumber Co., 22 A. B. R. 435, 169 Fed. 190): "It is contended that these notes were individual notes, and not partnership obligations, and were not provable pro rata with claims of partnership obligations; that in the execution of these notes in the form of individual obligations there was no mistake, accident, duress, or fraud; and that the notes were signed individually because the obligee "thought the individual signatures were really better than the company's signature." The preliminary objection that parol evidence was inadmissible to show that these notes were given for and on behalf of the partnership, on the ground that such evidence tended to contradict and vary the terms of written contracts, is not tenable. The evidence was not introduced for that purpose. There is no controversy as to the terms of written contracts. The question is: Whose contracts were they? Here are two individuals, whose names are signed to these notes. They were partners in business, and had been for many years. The holder of the notes introduced testimony tending to show that they were partnership notes, given for partnership obligations. This evidence was admissible under the well-known rule that evidence is always admissible to show that the signature to a written instrument, although that of an individual and prima facie for the purpose of acknowledging an individual liability, is in fact that of an agent for an undisclosed principal. * * * In other words, he thought that the notes signed by the individual partners for lumber furnished the business of the partnership constituted a partnership as well as an individual liability. The weight of authority appears to sustain such liability."

§ 2264. **Firm Debt Assumed by Partner Provable against Partner's Individual Estate.**—A firm debt may be assumed by one of the partners and become a provable debt against the individual estate of the partner.⁷

SUBDIVISION "C."

"PREFERENCES" AND "LEGAL LIENS" ON INDIVIDUAL PROPERTY IN PARTNERSHIP BANKRUPTCIES AND UPON PARTNERSHIP PROPERTY IN INDIVIDUAL BANKRUPTCIES.

§ 2265. **"Preferences" and "Legal Liens" on Individual Property Whether Nullified by Firm Bankruptcy; on Firm Property, Whether Nullified by Individual Bankruptcy.**—Liens by legal proceedings upon, and transfers of, the individual property of a member of a partnership, the partnership and not the individual member being in bankruptcy, and, conversely, liens by legal proceedings upon, and transfers of, partnership property in individual bankruptcies, are not, in general, affected by the provisions of the bankruptcy act relative to preferences and liens by legal proceedings obtained within four months of the bankruptcy; the firm and its individual members preserving their separate identities.⁸

7. In re Lehigh Lumber Co., 4 A. B. R. 221, 101 Fed. 216 (D. C. Pa.); In re Hirth, 26 A. B. R. 666, 189 Fed. 926 (D. C. Minn.).

8. American Steel & Wire Co. v.

Coover et al., 25 A. B. R. 58 (Sup. Ct. Okla.).

After dissolution by selling out to remaining partner, whether levy by partnership creditor a partnership lien, see ante, §§ 64, 171.

§ 2266. **Thus, "Preferences" and "Legal Liens" on Individual Property, Whether Affected by Partnership Bankruptcy.**—Thus, it would appear that transfers of the individual property of a partner or liens by legal proceedings thereon for individual debts are not voidable as preferences nor nullified as legal liens by the bankruptcy of the partnership.⁹ However, by § 5 of the Act, not only is the partnership trustee the trustee also for the individual estate, even where there is no individual adjudication, yet § 5 in clause "g" provides that the assets are to be so marshalled as to prevent "preferences" and to "secure the equitable distribution of the property of the several estates," from which it might be implied that the individual estates of nonbankrupt partners would be treated in this respect as if there had been an individual bankruptcy along with the partnership adjudication.¹⁰

§ 2267. **Thus, "Preferences" and "Legal Liens" on Partnership Property Not Affected by Bankruptcy of Partner.**—Partnership liens on partnership property are not voidable as preferences nor nullified as legal liens by the individual bankruptcy of one partner;¹¹ nor do bankruptcy proceedings against one partner affect the validity of a transfer made by the partnership.¹² Thus, preferences given by a partnership on partnership property that is being administered in the individual bankruptcy proceedings of one of the partners, are not affected.¹³

§ 2268. **Nor Transfers by Individual Partners Voidable as Preferences in Firm Bankruptcies, unless Individual Also Bankrupt.**—Nor, in general, are transfers by individual partners of individual assets voidable as preferences in partnership bankruptcies [unless the individual be also bankrupt or, perhaps, though not adjudged bankrupt he be insolvent and his estate be in process of administration in the firm bankruptcy by virtue of § 5].¹⁴

Obiter, Mills v. Fisher & Co., 20 A. B. R. 237, 159 Fed. 897 (C. C. A. Tenn.): "But it is not an act of bankruptcy for which a firm may be adjudged a bankrupt, that one of its members, out of his individual estate, prefers one of his own or one of the firm's creditors. * * * The application by one partner of his individual property to the payment of one firm creditor would be an

9. Impliedly, *In re Lehigh Lumber Co.*, 4 A. B. R. 221, 101 Fed. 216 (D. C. Pa.).

But compare principle underlying *In re Stokes*, 6 A. B. R. 262, 106 Fed. 312 (D. C. Pa.).

10. Compare on principle, *Francis v. McNeal*, 228 U. S. 695, 30 A. B. R. 244.

11. *McNair v. McIntyre*, 7 A. B. R. 638, 113 Fed. 113 (C. C. A. N. Car.); *American Steel & Wire Co. v. Coover*, et al., 25 A. B. R. 58 (Sup. Ct. Okla.).

Compare, *Smedley v. Speckman*, 19

A. B. R. 694, 157 Fed. 815 (C. C. A. Pa.), where court found existence of partnership not proved.

12. *McNair v. McIntyre*, 7 A. B. R. 638, 113 Fed. 113 (C. C. A. N. C.).

13. As to whether a preference by a firm is voidable in the individual bankruptcy of one partner to whom the others have subsequently sold out, see post, § 2265, et seq.

14. *Miller v. Acid & Fertilizer Co.*, 21 A. B. R. 416, 211 U. S. 496. *Obiter, Mayes v. Palmer*, 31 A. B. R. 225, 208 Fed. 97 (C. C. A. Mo.).

individual act and not the joint act of the firm, and, therefore, not an act for which the firm could be adjudged bankrupt."

But a transfer of individual assets by one member to pay a firm creditor a greater percentage than another firm creditor would get from the same individual estate may be a preference, since the individual estates constitute sub modo funds to which partnership creditors are entitled to resort, in proper order of priority after individual creditors are satisfied in full, so that a transfer to one firm creditor without a like transfer to other firm creditors would be the giving of a greater percentage to one creditor than to another of the "same class" in the order of priority.¹⁵

And by state law such an individual transfer may be a voidable preference in a partnership bankruptcy of which the trustee in bankruptcy may avail himself by subrogation to the rights of any creditor who has already instituted proceedings.¹⁶

§ 2268½. Retiring Partner's Mortgage on Partnership Assets for Unpaid Purchase Price, Preference in Partnership Bankruptcy.—A mortgage given on firm assets within four months of the bankruptcy of the firm to secure a retiring partner for the unpaid purchase price of his share, is a partnership preference.¹⁷

SUBDIVISION "D."

TRANSFER OF PARTNERSHIP INTEREST TO COPARTNER OR THIRD PERSON.

§ 2269. First, Where One Partner in Insolvent Firm Sells Out to Other Who Thereafter Becomes Bankrupt.—Retiring partners may, effectually, sell not only their firm interests but also the specific property of the partnership to a remaining partner who assumes the debts, even though insolvent, and thus convert firm property into individual property; for the correct doctrine is that until partnership property is placed in the custody of the law by some suit or act which invokes the interposition of a court to administer it, partners, with the consent of each, have the right and the power to convert it into individual property, to apply it to the payment of individual debts in preference to the payment of partnership debts, or to make any other disposition of it in good faith which does not constitute a voidable preference; and that insolvency does not destroy or diminish this right of disposition; that the right of the creditors of the partnership to be paid out of the partnership property in preference to the individual creditors does not attach until an application is made to some court for the ad-

15. *Mills v. Fisher & Co.*, 20 A. B. R. 237, 159 Fed. 897 (C. C. A. Tenn.), quoted at § 1291. Compare, *Speckman v. Smedley Bros.*, 18 A. B. R. 717, 153 Fed. 771; also compare, ante, §§ 171, 1387½.

16. *Miller v. Acid & Fertilizer Co.*, 21 A. B. R. 416, 211 U. S. 496.

17. *In re Floyd & Co.*, 19 A. B. R. 438, 156 Fed. 206 (D. C. N. Car.); analogously, compare, *In re Stoddard Bros. Lumber Co.*, 22 A. B. R. 435, 169 Fed. 190 (D. C. Idaho), affirmed, sub nom., *Mock v. Stoddard*, 24 A. B. R. 403, 177 Fed. 611 (C. C. A. Idaho).

ministration of the partnership property; nor even then unless some partner has at that time such right, the preferential equity of the partners being the mere right to enforce the right of the partners to compel such a preference; in short, that, before the partnership property is placed in custodia legis it is not held in trust for the partnership creditors and they have no lien upon it; and that the covenant of the remaining partner to pay the firm debts, though both he and the firm are insolvent is a sufficient consideration; and that the assumption of payment of partnership debts by one partner in consideration of an absolute transfer to him of the partnership property by the other creates no trust in and fastens no lien upon the property thus transferred in favor of the partnership creditors prior to any application to a court to interpose and assume administration of the property.

Sargent v. Blake, 20 A. B. R. 115, 160 Fed. 57 (C. C. A. Mo.): "There are two rules of law which at different times apply to the management and disposition of the property of a partnership, first, partners own, and, with the consent of each, have the right and power to sell and dispose of the partnership property, to transform it into the individual property of one or more of the partners, to apply it or its proceeds to the payment of their individual debts in preference to those of the partnership, and to make such other honest disposition of it as they deem fit; second, in the administration of the property of a partnership in the courts the creditors of the partnership have the right to the application of the partnership property to the payment of the partnership debts in preference to the individual debts of the respective partners. The first is a rule of operation, the second a rule of administration. The first governs during the operation of the partnership business and the disposition of the partnership property by the partners, the second operates during the administration of the partnership property after it is brought into the custody of a court. The first rule prevails until by some suit or act the interposition of some court is invoked to administer the partnership property, and until that time the second rule is ineffective. Before the partnership property is placed in custodia legis for administration, it is not held in trust for the payment of the partnership creditors in preference to the creditors of the individual partners. The partnership creditors have no lien upon it, and no independent right to its application to the payment of their claims in preference to the claims of the creditors of the individual partners. Each partner, however, has the right to require the partnership property to be applied to the payment of the partnership debts in preference to the debts of the individual partners, to the end that he may not be required to pay the former out of his individual estate. The right of the creditors of the partnership to payment out of the partnership property in preference to the individual creditors is the mere right by subrogation or derivation to enforce this right of one of the partners after the partnership property has been placed in the custody of the law. Until it has been so placed each partner has plenary power at any time to release or waive this right, and if each partner has done so and at the time the property comes within the jurisdiction of a court no partner has this right, then no creditor of the partnership has it, for a stream can not rise higher than its source."

Nor do the provisions of § 5 of the Bankruptcy Act cause a different rule to prevail in bankruptcy.

Sargent v. Blake, 20 A. B. R. 115, 160 Fed. 57 (C. C. A. Mo.): "The clause of § 5f upon which counsel rely is nothing but the familiar rule of administration of partnership and individual estates which has been imported into the bankruptcy law from the courts of equity. 'The net proceeds of the partnership property shall be appropriated to the payment of the partnership debts, and the net proceeds of the individual estate of each partner to the payment of the individual debts.' The partnership property and the individual estate at what time, four months, or at some indefinite time within four months before the petition is filed, or at the time it is filed? This section treats of administration in the bankruptcy court and hence of the partnership and individual property, the title to which is in the bankrupt at the time the petition against him is presented to the court and that which he had transferred in fraud of his creditors. Section 70. Any other interpretation would produce intolerable vexation and confusion, for in the daily conduct of business, partners are necessarily and constantly applying partnership property to the payment, not only of large individual obligations, but to the payment of their petty individual debts, for living expenses, and are often devoting their individual property to the promotion of the partnership business and the discharge of the partnership debts. It never could have been, it never was, the intention of Congress that these transactions—these transformations of partnership into individual and of individual into partnership property within four months, or within any other time preceding the commencement of bankruptcy proceedings—should either be rescinded or avoided by subsequent adjudications in bankruptcy unless they were actually fraudulent or voidably preferential. It did not make them fraudulent in themselves. The terms of § 5f and the natural and rational interpretation of them in the light of the general rules of law and of the entire act in which they appear, limit their application to partnership and individual property at the commencement of bankruptcy proceedings, and to property the transfer of which is fraudulent for other reasons than that partnership property was applied to the payment of individual debts, or individual property to the payment of partnership debts. This conclusion is in accord with the general principles applicable to the management and disposition of partnership property."

Such right of the firm creditor to pursue firm assets into the hands of the remaining partner after dissolution and sale of the outgoing partner's interest, is purely derivative, the creditor deriving his rights through the right of the outgoing partner to have the assets first applied to partnership debts; so that if the outgoing partner has relinquished this right the creditor has no right to which he may be subrogated.¹⁸

Fitzpatrick v. Flannagan, 106 U. S. 648: "The legal right of a partnership creditor to subject the partnership property to the payment of his debt consists simply in the right to reduce his claim to judgment, and to sell the goods of his debtors on execution. His right to appropriate the partnership property specifically to the payment of his debt, in equity, in preference to creditors of an individual partner, is derived through the other partner, whose original right it is to have the partnership assets applied to the payment of partnership obligations. And this equity of the creditor subsists so long as that of the partner through which it is derived remains; that is, so long as the partner himself 'retains an interest in the firm assets, as a partner, a court of equity will allow the creditors

18. *Huiskamp v. Wagon Co.*, 121 U. S. 310; *Cave v. Beauregard*, 99 U. S. 125.

of the firm to avail themselves of this equity, and enforce through it the application of those assets primarily to payment of the debts due them, whenever the property comes under its administration.' Such was the language of this court in *Case v. Beauregard*, 99 U. S. 119, 25 L. Ed. 370, in which Mr. Justice Strong, delivering the opinion, continued as follows: 'It is indispensable, however, to such relief, when the creditors are, as in the present case, simply contract creditors, that the partnership property should be within the control of the court, and in the course of administration, brought there by the bankruptcy of the firm, or by an assignment, or by the creation of a trust in some mode. This is because neither the partners nor the joint creditors have any specific lien, nor is there any trust that can be enforced until the property has passed in *custodiam legis*.' Hence it follows that 'if, before the interposition of the court is asked, the property had ceased to belong to the partnership, if by a bona fide transfer it has become the several property of one partner or of a third person, the equities of the partners are extinguished, and consequently the derivative equities of the creditors are at an end.'"

Such outgoing partner, for instance, will be held to have waived his right to insist upon application of the former firm assets to firm debts where both the partners unite in selling to a third person.¹⁹

Again, the outgoing partner may relinquish his right to have the firm assets applied to the firm debts by expressly applying the firm property to individual debts, in which event the firm creditor again has no right to which he may be subrogated.²⁰

The same rule, namely, that the creditors' right is a derivative right, applies where the partnership was solvent when the sale was made.

In *re Filmar* (*Lippincott v. Klosterman*), 24 A. B. R. 194, 177 Fed. 170 (C. C. A. Ill.): "Swigert, a merchant tailor, in October, 1905, sold a third interest in his business to Filmar. The firm of Swigert & Filmar continued the business till January 8, 1906, when Swigert sold his interest to Filmar in consideration of a small money payment and Filmar's agreement to pay the partnership debts and save Swigert harmless therefrom. Partnership assets were then in excess of partnership debts. By payment and novation Filmar very shortly settled all partnership debts except one to appellant Lippincott. Lippincott refused to accept Filmar as debtor in place of the partnership, and proceeded to press Filmar for payment. Filmar, by various promises and representations, warded off Lippincott until February 20, 1906, when he filed his voluntary petition in bankruptcy. The property scheduled by Filmar and turned over to the trustee had all been property of the partnership. The scheduled debts were all separate individual debts of Filmar's except the debt to Lippincott. Thereupon Lippincott filed his petition, asking that his debt be paid from the assets ahead of the claims of Filmar's individual creditors; and Swigert filed a like petition, asking the same relief, without offering to repay the consideration he received on selling his interest

19. In *re Terens*, 23 A. B. R. 680, 175 Fed. 495 (D. C. Wis.); *Huiskamp v. Wagon Co.*, 121 U. S. 310; *Fitzpatrick v. Flannagan*, 106 U. S. 648; *Case v. Beauregard*, 99 U. S. 119.

20. *Sargent v. Blake*, 20 A. B. R. 115, 160 Fed. 57 (C. C. A.); In *re Terens*, 23 A. B. R. 680, 175 Fed. 495

(D. C. Wis.); *Thayer v. Humphrey*, 91 Wis. 276.

Instance, where outgoing partner had not relinquished the equity, In *re Filmar* (*Lippincott v. Klosterman*), 24 A. B. R. 194, 177 Fed. 170 (C. C. A. Ills.), quoted post.

to Filmar. The final decree dismissed these petitions for want of equity; and the petitioners have severally appealed. With the property in custody and all the parties present, and no rights of innocent purchasers or transferees having intervened, a court of general equity powers would concededly award priority to Lippincott, because there had been no application of the property with the consent of the partners, to the payment of individual debts (*Sargent v. Blake* (C. C. A., 8th Cir.), 20 Am. B. R. 115, 160 Fed. 57, * * *) because Lippincott in his own right as a partnership creditor would be entitled to equity's rule of distribution, and because Swigert for his own protection would have the right to ask that Lippincott be first paid. Was there less power in the bankruptcy court? Section 5a * * * declares that: 'A partnership, during the continuation of the partnership business, or after its dissolution and before the final settlement thereof, may be adjudged a bankrupt.' Section 5f explicitly adopts the equity rule of administration. Section 5g authorizes the bankruptcy court to 'marshal the assets of the partnership estate and individual estates so as to prevent preferences and secure the equitable distribution of the property of the several estates.' These provisions, we think, indicate very clearly that Congress intended that the bankruptcy courts should have full equity powers in dealing with partnership matters."

Of course, where the outgoing partner has not relinquished his equity but joins with the firm creditors in asking precedence for firm debts, the firm debts will have precedence.²¹

On the contrary, it has also been held that the partnership creditors' lien upon, or rights in, partnership assets follow the assets into the hands of a remaining partner who has bought out his copartners, and that such creditors are entitled to priority of payment therefrom over individual creditors of the remaining partner, upon his bankruptcy.²² This is presumably on the doctrine that the transfer by one partner of his partnership interest to another is not the transfer of title to any specific assets but a transfer of an individual interest in any surplus left after satisfaction of firm obligations; and that thus, although the rights of creditors must be worked out through the partners and rise no higher than those of the partners, yet, in effect, precisely by virtue of the sale itself a lien exists in favor of firm creditors. When partnership property is thus converted into individual property by the sale to one partner of all the other partners' interest, it is not a sale of specific articles but a sale of a share in the surplus after all firm debts are paid. In effect, a lien in favor of firm creditors is thereby created or maintained, and is so created precisely through the acts of the partners themselves.

In *re Terens*, 23 A. B. R. 680, 175 Fed. 495 (D. C. Wis.): "On the other hand, it is contended, and the referee ruled, that by virtue of the dissolution agreement of December 15th *Terens* became the sole owner, and that there is now no partnership fund to be administered. * * * Under these

²¹ In *re Filmar*, 24 A. B. R. 194, 177 Fed. 170 (C. C. A. Ill.), quoted *supra*.

²² In *re Damare*, 28 A. B. R. 297, (Ref. Miss.).

Whether a levy by a firm creditor on former firm property is a firm levy

sufficient to warrant the adjudication of the firm, see *Holmes v. Baker & Hamilton*, 20 A. B. R. 252, 160 Fed. 922 (C. C. A. Wash.); also, see *ante*, §§ 64, 65½, 171.

circumstances, what was the legal effect of the dissolution agreement? What did Oswald sell? It was not specific articles of personal property. It was not a transfer of the corpus of the estate, but of only such interest in the surplus after the firm debts had been provided for. At the outset the distinction must be sharply drawn between such a transfer by one insolvent partner to another, and a sale by both partners of certain specific property to a third party. In the latter case the entire title passes by the transfer, and it has been repeatedly held that the legal right of either or both partners to sell the firm assets and transfer good title thereto is not impaired by the fact of insolvency. In my judgment the dissolution agreement, under the peculiar circumstances of this case, did not work a liberation of the firm assets and convert the same into the individual assets of Terens, but that, when the property came to the custody of the court, Oswald still retained the right to insist upon the payment of the firm debts out of the firm assets, as he does by his consent to the administration by the court, and that by subrogation or derivation the firm creditors are justified in insisting upon such a marshaling of assets as is provided for in the Bankruptcy Act."

In *re Mosier*, 7 A. B. R. 268, 112 Fed. 138 (D. C. Vt.): "Partners in an insolvent partnership have no interests of their own in the partnership property, but the whole is subject to the lien of the partnership creditors.

In *re Gillette*, 5 A. B. R. 123, 104 Fed. 769 (D. C. N. Y.): "The transfer of the partnership interest by Prentice to Gillette does not deprive creditors of the right to hold partnership assets for payment of their claims; and creditors having claims against an insolvent debtor who is a member of a copartnership can not, where the debtor has been adjudicated bankrupt, receive dividends from partnership assets until the copartnership creditors have been paid in full.

Compare analogously, *obiter*, *Deaf and Dumb Institute v. Crockett*, 17 A. B. R. 241, 117 App. Div. N. Y. 269: "It is well settled that the interest of an individual member of a firm may be assigned by him, but the assignee only acquires the proportionate share of the member in the surplus remaining after the payment of the copartnership debts and the adjustment of the equities between the members of the firm, and does not acquire any title to the corpus of the firm assets, which remain a primary fund for the payment of firm debts with the right in the assignor as well as in the creditors to compel their appropriation thereto." [Of course, if the above is limited to an assignment to a stranger, it is not contrary to the doctrine set out in the beginning of this section, since in that event the partner still retains his right to have the firm assets first applied to the firm debts, and upon bankruptcy intervening the firm creditors would be subrogated to this right.]

§ 2270. But if Partnership Creditors Assent to Assumption They Become Individual Creditors.—But, of course, in any event, if the partnership creditors assent to the assumption of the partnership debts by the remaining partner, they become thereby his individual creditors and lose their lien.²³

In *re Denning*, 8 A. B. R. 133, 114 Fed. 219 (D. C. Mass.): "It seems that a former joint creditor, who has elected to become a separate creditor of the bankrupt, assents to the conversion of the joint into separate assets, and is permitted to come upon the converted estate as a separate creditor."

²³. [1867] In *re Johnson*, Fed. Cas. 7,369.

Compare, instance where partnership creditor did not assent, In *re*

Filmar (*Lippincott v. Klosterman*), 24 A. B. R. 194, 177 Fed. 170 (C. C. A. Ill.), quoted at § 2269.

And the assent is sufficient if not made until bankruptcy has intervened.²⁴

In *re Keller*, 6 A. B. R. 336, 109 Fed. 118 (D. C. Iowa): "Counsel for the claimant take the position that the payment of the \$171.70 on October 2, 1900, was made by the firm of Keller & Stake; that the partnership has not been adjudged a bankrupt; and that, as the court in bankruptcy has before it only the individual estate of Almon D. Keller, it cannot deal with payments made by the pre-existing firm of Keller & Stake, nor can it undertake to marshal the firm and individual assets in this proceeding. The fact, however, that the partnership has not been adjudged a bankrupt, prevents the question of the marshaling of assets from arising in this case. The claimant, as shown by the proof of debt filed by it, assumes the position of a creditor of Almon D. Keller. There is no case before the court in which it can undertake to separate the debts and property of a firm from that of the individual partners, as is provided for in § 5 of the Bankrupt Act. When J. P. Stake sold his interest in the partnership to Keller, the property became the individual property of the latter, and it passed, as such, to his trustee in the bankruptcy proceedings. Neither Stake nor the firm creditors have initiated any proceedings for the enforcement of any supposed equities or rights in the property formerly belonging to the firm, and therefore the referee rightly ruled that the claims filed by the company could only be viewed as a claim against Keller. * * * In the case now under consideration there was a valid transfer of the partnership property to Almon D. Keller. This transfer has not been questioned by any one. When Keller went into Bankruptcy, he did so as an individual, and he transferred to the trustee all his property, including that which had formerly belonged to the firm of Keller & Stake. Under these circumstances, the court in bankruptcy cannot deal with the estate in any other light than as the individual estate of Almon D. Keller. The claims of the creditors of the late firm of Keller & Stake can be proved only as claims against the bankrupt, and this is what was done by the claimants in this case; for, as already stated, in the proof of claim filed before the referee the averment is that 'Almon D. Keller, the person by whom a petition for adjudication in bankruptcy has been filed, was at and before the filing of said petition, and still is, justly indebted to said corporation in the sum of \$563.94;' and it is thus made clear that the claimant bases its right to share in the estate on the ground that it occupies the position of a creditor of the individual, Almon D. Keller, and its rights are just what they would be if the business had always been carried on by Keller as an individual."

§ 2270½. Where Outgoing Partner's Relinquishment of Right to Apply on Firm Debts Is in Bad Faith or Would Work Preference.—

There is to be recognized a modification, in bankruptcy and insolvency law, to the general rule that the firm creditors' right to pursue former partnership assets into the hands of an individual purchasing partner, is merely derivative and such that it may be relinquished by the acts of the outgoing partners. This modification is that such relinquishment will not be valid to deprive the firm creditor of the right to pursue them where the relinquishment was made in bad faith or to effect a "preference" of individual creditors over firm creditors, "preference" in this connection referring not to the technical preference defined in § 60 of the bankruptcy law, but referring, rather, to the broader meaning of preference.

24. [1867] In *re Johnson*, Fed. Cas. 7,369.

Thus, the Bankruptcy Act itself, in § 5 (g) says that the court "may marshal the assets of the partnership estate and individual estates so as to prevent preferences and secure the equitable distribution of the property of the several estates," the use of the word "preferences" in connection with "equitable distribution" seeming to indicate that the preferences here referred to are not the technical preferences defined in § 60 of the Bankruptcy Act.²⁵

In *re Denning*, 8 A. B. R. 133, 114 Fed. 219 (D. C. Mass.): "Moreover, § 5g of the Bankruptcy Act was intended to clear up the whole matter, and to permit the court to deal with conversions of this kind so as not only to prevent preferences in the technical meaning of that word, but also so as to secure the equitable distribution of the property of the several estates."

In *re Terens*, 23 A. B. R. 680, 175 Fed. 495 (D. C. Wis.): "It remains to consider and construe § 5g, which is in *pari materiae*, which throws much light on the amplitude of the equitable jurisdiction conferred upon the court. It allows proof of the partnership estate against the individual estate, and vice versa. It expressly suggests the doctrine of marshaling assets to prevent preferences and to secure the equitable distribution among the several estates. The preferences supposed to interfere with a just and equitable distribution may result from the action of partners calculated to convert partnership property into individual assets, thus giving undue advantage to individual creditors. Properly construed, this subdivision meets the very case we have in hand."

Thus, the question sifts down largely to one of good faith. If the transfer be in bad faith towards the firm creditors, it would not be effective to deprive them of their derivative right.

What will amount to bad faith toward firm creditors in this regard is not very clearly outlined. It has been held that a dissolution by insolvent partners, within the four months preceding bankruptcy, where such partners know they are insolvent and which is made to enable the individual creditors of one or both partners to get an advantage over the firm creditors, will be such bad faith as will bring the case under the rule.²⁶

Indeed, in many cases, under varying circumstances, transfers by one partner to another have been held to be *mala fide*, without proof of actual fraudulent intent.²⁷

However, where the outgoing partner has not relinquished his equity, no proof of bad faith is requisite on the part of the firm creditor, especially where the outgoing partner joins with the creditor in asking that firm assets be applied first to firm debts.²⁸

²⁵. In *re Wilcox*, 2 A. B. R. 117, 94 Fed. 84 (D. C. Mass.), quoted at § 2257; In *re Head & Smith*, 7 A. B. R. 556, 114 Fed. 489 (D. C. Ark.); In *re Jones & Cook*, 4 A. B. R. 141, 100 Fed. 781 (D. C. Mo.).

²⁶. In *re Terens*, 23 A. B. R. 680, 175 Fed. 495 (D. C. Wis.); In *re Jones & Cook*, 4 A. B. R. 141, 100 Fed. 781

(D. C. Mo.); In *re Worth*, 12 A. B. R. 566, 130 Fed. 937 (D. C. Iowa). Compare, on the facts, In *re Damare*, 28 A. B. R. 297 (Ref. Miss.).

²⁷. In *re Terens*, 23 A. B. R. 680, 175 Fed. 495 (D. C. Wis.).

²⁸. In *re Filmar*, 24 A. B. R. 194, 177 Fed. 170 (C. C. A. Ill.), quoted at § 2269.

§ 2271. **Where Sale Made to Enable Remaining Partner to Claim Exemptions.**—Where the sale is made to enable the remaining partner to claim exemptions from the property, the sale has been held by some courts to be void and the fund formerly belonging to the partnership to be subject to the pursuit of the partnership creditors.²⁹

But the better rule would seem to be that, if the sale otherwise be bona fide, it would not be invalidated by the mere fact that it was made to enable the remaining partner to claim his exemptions.

Such, at any rate, would appear to be the logical result of an adherence to the rule enunciated ante, in § 2270¹/₂ and is the rule in similar situations, adopted in state court decisions.³⁰

29. In *re Head & Smith*, 7 A. B. R. 556, 114 Fed. 489 (D. C. Ark.): In this case the court said the transfer amounted to a "preference" to individual creditors. This is clearly wrong. A preference to be such must be to a creditor of the bankrupt, but such transfer as was made in this case does not operate to give any creditor of the bankrupt partnership a preference; its effect is to take away all property from all partnership creditors until the individual creditors of the remaining partner are satisfied.

In *re Rosenbaum*, 1 N. B. N. 541 (Ohio); In *re Bergman*, 2 N. B. N. & R. 806; In *re Rudnick*, 2 N. B. N. & R. 769; In *re Rudnick*, 4 A. B. R. 531 (D. C. Wash., reversing 2 N. B. N. & R. 769).

It has been held, in one case, that any scheme or device resorted to by persons in contemplation of bankruptcy for the purpose of charging partnership assets with the individual liabilities of the partners, is violative of the provisions of the bankruptcy act, § 5 (g). In *re Jones & Cook*, 4 A. B. R. 141, 100 Fed. 781 (D. C. Mo.); compare, In *re Denning*, 8 A. B. R. 133, 114 Fed. 219 (D. C. Mass.).

Compare, In *re Worth*, 12 A. B. R. 566, 130 Fed. 927 (D. C. Ia.): In this case shortly before the adjudication of a partnership and its individual members, the firm was dissolved by mutual consent, one partner retaining its assets and assuming its liabilities. The court held that the assets were first liable in bankruptcy under § 5f, for his individual debts, and while this would be inequitable as to nonassenting firm creditors, they could not, at the same time, affirm the dissolution agreement in so far as it made the remaining partner an individual debtor of a firm creditor at dissolution, and

disaffirm or repudiate it so far as it was a transfer of the firm assets, in consideration of the assumption of firm debts; that the nonassenting creditor must either affirm or disaffirm the transaction as a whole; the court further holding that in such case, where the receiver of the creditor bank surrendered all preferences he had under a chattel mortgage upon the stock of merchandise formerly belonging to the firm, and an assignment of account due it, given by the purchasing partner within the four months period, the proceeds of the assets of the firm and its individual members should be distributed as though no dissolution had taken place. The court finally says:

"It will be more equitable to hold that the relation of the creditors of the copartnership and of the individual members thereof to the partnership assets are not changed by this transaction of Oct. 16 and that the proceeds of the assets of the firm and its individual members should be distributed as though such transaction had not taken place."

Compare, In *re Gillette*, 5 A. B. R. 123, 104 Fed. 769 (D. C. N. Y.).

30. On the other hand there is strength to the reasoning that the transfer is not voidable, but that the former partnership property should be applied to the payment of partnership debts and be treated precisely as if still partnership property, so far as partnership creditors who have not assented to the assumption of the old firm debts by the continuing partner are concerned (precisely as in cases of the assignment of a partner's interest to a stranger), but as to all others it should be treated as the bankrupt's individual property. Compare, suggestively, *obiter*, *Deaf & Dumb Institute v. Crockett*, 17 A. B. R. 233, 117 App. Div. N. Y. 269.

And that such remaining partner of

§ 2272. Retiring Partner, Surety for Remaining Partner, Entitled to Subrogation to Debts He Pays.—Such retiring partner becomes surety for the remaining partner and is entitled to subrogation to such debts as he is compelled to pay.

In *re* Dillon, 4 A. B. R. 63, 100 Fed. 627 (D. C. Mass.): "In equity, the relation of McGuire to Dillon concerning the debts of the old firm was that of surety. By this contract with McGuire, Dillon made himself primarily responsible for the payment of the firm debts. As regards Claflin, McGuire remained primarily liable, together with Dillon; but, as regards Dillon, McGuire was only a surety. That the relation between the two former partners is that of principal and surety is recognized in bankruptcy. * * * As to the bankrupt's estate, therefore, McGuire stands as a surety who has paid the debt of his bankrupt principal subsequently to the adjudication."

Compare, to same effect, In *re* Carmichael, 2 A. B. R. 815, 96 Fed. 594 (D. C. Iowa): "By the purchases made by him of the judgments entered against the firm of which he was a member, he discharged the liability of the firm to the judgment creditors, but became a creditor of his copartners for their respective shares of the money by him advanced in the purchase and discharge of these judgments, and the mere fact that he procured assignments in writing to himself of the judgments in question does not change his position with respect to his copartners."

But the claim of a solvent partner arising from his liquidation of the firm business, is not a valid debt against the estate of the bankrupt partner, who, at the time of adjudication, was not indebted either to the firm nor to the liquidating partner.³²

§ 2273. But Retiring Partner's Claim for Purchase Price of Share, Not to Compete with Firm Creditors in Individual Estate of Remaining Partner.—But the retiring partner's claim for the purchase price of his partnership interest should not share in the old firm assets;³³ nor in the individual assets of the remaining partner, until after the firm creditors have been satisfied; for he should not be permitted to compete with his own creditors.³⁴

§ 2274. Whether "Preferential" Transfer by Partnership Voidable Where Remaining Partner Alone in Bankruptcy.—Where the

course would not be entitled to exemptions out of the partnership property as against the partnership creditors, compare, In *re* Mosier, 7 A. B. R. 268, 112 Fed. 138 (D. C. Vt.); compare inferentially, In *re* Head & Smith, 7 A. B. R. 556, 114 Fed. 489 (D. C. Ark.).

³² In *re* Walker, 23 A. B. R. 805, 176 Fed. 455 (D. C. Ala.).

³³ Compare ante, § 2247½; In *re* Stoddard Bros. Lumber Co., 22 A. B. R. 435, 169 Fed. 190 (D. C. Idaho); *Mock v. Stoddard*, 24 A. B. R. 403, 177 Fed. 611 (C. C. A. Idaho, affirming In *re* Stoddard Bros. Lumber Co., 22 A. B. R. 435, 169 Fed. 190.).

³⁴ In *re* Denning, 8 A. B. R. 133, 114 Fed. 219 (D. C. Mass.); In *re* Gerson, 5 A. B. R. 480 (Ref. Pa. affirmed by D. C.). Compare, In *re* Rice, 21 A. B. R. 205, 164 Fed. 514 (D. C. Pa.).

Retiring Partner's Mortgage on Insolvent Firm Assets Given within Four Months for Unpaid Purchase Price of Share, Preference in Firm Bankruptcy.—A mortgage given on partnership assets within the four months of the partnership bankruptcy to secure a retiring partner for the unpaid purchase price of his share is a partnership preference, see ante, § 2268½.

bankrupt partner has assumed the liabilities and taken the assets of the partnership, it is a question whether a transfer that would have been a preference were the firm in bankruptcy will be a preference in the individual bankruptcy of the partner. It has been held that the effect of a preference by a firm cannot thus be avoided by the conversion of the firm assets into individual assets and the bankruptcy of the remaining partner.³⁵

But the better rule would seem to be that creditors of the firm, in order to preserve their rights against a firm preference, should file a petition in bankruptcy against the firm, and assert the lien of partnership debts on the old firm assets.

A secret agreement whereby, on the dissolution of a partnership, one of the partners, who continued the partnership business, was to dedicate certain book accounts to the payment of specific firm obligations, will not be enforced in bankruptcy where there was no actual transfer or appropriation of the accounts.³⁶

§ 2275. Second, Where One Partner of Insolvent Partnership Sells Out to Other and Himself Becomes Bankrupt.—Where one partner of an insolvent partnership sells out to the other and later himself becomes bankrupt, such sale is valid, and the former partnership assets cannot be administered in bankruptcy, without the other partner's consent.³⁷

And the sale is valid, even though the sum realized is used in paying off some of the bankrupt's own creditors; and the remaining partner is entitled to the partnership assets, although the bankrupt was still in their actual custody as manager for the purchaser.³⁸

§ 2276. Third, Where Partnership Interest Transferred to Third Person, Partner Becoming Bankrupt.—Third, where partnership interests are transferred to third persons, and either or both partners become bankrupt, the transfer is to be treated as a transfer by an individual of his individual assets.

The rights of firm creditors are not impaired. The transfer is of a share in merely the surplus after payment of firm debts;³⁹ and follows the rules laid down in the preceding paragraphs.

35. In re Keller, 6 A. B. R. 334, 109 Fed. 118 (D. C. Iowa). But compare, § 2268.

36. In re Wilson, 27 A. B. R. 867, 194 Fed. 564 (D. C. Pa.).

37. See ante, § 2251, et seq. In re Kindt, 4 A. B. R. 148, 101 Fed. 107 (D. C. Iowa).

38. In re Kindt, 4 A. B. R. 148, 101 Fed. 107 (D. C. Iowa).

39. Obiter, Deaf & Dumb Institute v. Crockett, 17 A. B. R. 240 (N. Y. Sup. Ct. App. Div.). Compare, In re Bo-

relli & Callhan, 16 A. B. R. 115, 142 Fed. 296 (D. C. Conn.).

Compare, In re English, 10 A. B. R. 133 (D. C. N. Y., reversed on other grounds, in 11 A. B. R. 674, 127 Fed. 750). This was a case, however, of the transfer by both partners of an undivided one-half interest in the firm assets (apparently not an interest in the partnership but only in its assets) to a creditor, the wife of one of the partners, to pay a debt, more than four months before bankruptcy of the partnership, and was held valid.

DIVISION 6.

SUBROGATION TO RIGHTS OF VARIOUS PARTIES IN THE DISTRIBUTION OF ASSETS.

SUBDIVISION "A."

SUBROGATION BY ASSIGNMENT OF CLAIMS AFTER BANKRUPTCY.

§ 2277. Subrogation by Assignment of Claims after Bankruptcy.

—The subject of the assignment of claims in accordance with the provisions of the Bankruptcy Act and the General Orders in Bankruptcy, has been previously discussed.⁴⁰

SUBDIVISION "B."

EQUITABLE SUBROGATION UNDER ORDINARY RULES.

§ 2278. Subrogation by Agreement with Bankrupt or Creditor.

—Where one pays a debt of the bankrupt with an understanding, made either with the bankrupt or the creditor, that he shall be subrogated to the creditor's claim, he will be so subrogated in bankruptcy.⁴¹

Thus, one furnishing the bankrupt money to pay a secured note, at the bankrupt's request, and under promise to turn over the notes paid thereby, is entitled to subrogation.⁴² Also, an arrangement with a corporation which is taking over the bankrupt's assets and business, and which is anxious to retain a certain agent's favor, to forward to the agent the remainder of certain goods contracted for with the bankrupt, with the understanding that the agent's claim should be presented against the bankrupt and the dividend be turned over to the purchasing company, amounts to a purchase or agreement for subrogation and not to a payment, although the words used in the forwarding were "in liquidation" of the agent's claim.⁴³ But the furnishing of money to a bankrupt corporation to pay its pay roll, under an agreement with the corporation that the pay roll should be assigned, but where the pay roll was not actually assigned, has been held, but improperly, not to entitle the person so advancing to an equitable subrogation to the pay roll.⁴⁴ It would seem that the advancement under the agreement created the equity of subrogation, whether the assignment was actually carried out or not, so long as there was no waiver. The taking of workmen's pay checks in part payment of provisions furnished to them, no agreement for assignment existing but a mere supposition being indulged in between the storekeeper and the bankrupt that as matter of law the storekeeper would

40. See ante, "Assigned Claims," § 608, et seq.

41. In re Lee, 25 A. B. R. 436, 182 Fed. 579 (C. C. A. Kan.).

42. In re McGuire, 13 A. B. R. 704, 137 Fed. 967 (D. C. Ohio).

43. Haas-Barnick Co. v. Poruondo, 15 A. B. R. 130, 138 Fed. 949 (D. C. Pa.).

44. In re Carolina Car Co., 11 A. B. R. 488, 127 Fed. 178 (D. C. N. Car.). Similarly, but not identically, United Surety Co. v. Iowa Mfg. Co., 24 A. B. R. 726, 179 Fed. 55 (C. C. A. Mo.).

stand in the shoes of the workmen, was held to be no assignment and not to entitle the storekeeper to subrogation.⁴⁵

Although a pledge, given to secure money used by the bankrupt to pay the purchase price of manufactured goods and relieve the goods from the lien of the artisan upon them, may have been itself made without authority, yet the person advancing the money by agreement with the bankrupt is entitled to subrogation to the artisan's lien, and the trustee takes the property subject to such right of subrogation.⁴⁷

Where the bankrupts were loggers and failed to pay their workmen, and the owners of the logs paid off the workmen's liens to prevent threatened foreclosure and sale, and the time checks representing each man's claim were turned over to the owners of the logs upon such payment, the transaction entitled the owners of the logs to subrogation to the workmen's liens, even if the transaction did not constitute an out and out assignment.⁴⁸

§ 2279. Whether Subrogation to Workmen's Priority Claims to Compete with Workmen's Own Later Claims.—But it has been held that subrogation to workmen's priority claims will not be permitted to take precedence over workmen's own later priority claims, where the understanding was not with the workmen but solely with the bankrupt.

Browder & Co. v. Hill, 14 A. B. R. 619, 136 Fed. 821 (C. C. A. Tenn.): "Appellants do not claim in their petition or assignment of error or briefs that there has been any assignment of the labor claims pro tanto by consent or knowledge of the laborers themselves.

"In the absence of evidence that the owners of such lien claims intended to sell and agreed that the lien should be kept alive for the benefit of the purchaser, payment and not an assignment will be presumed. *Fenner v. F. L. & T. Co.*, 90 Fed. 349.

"There is therefore no foundation for any claim that appellants are assignees of the claims or lien in behalf of labor claims under any agreement, express or implied, with the creditors themselves.

"What they do claim is, that there existed an express agreement with the debtor, the Furnace Company, that such claims when paid off by them 'should stand against the Furnace Company in the same attitude as if held by the original wage earners.'

"The mere fact that one pays off a debt at the instance of the debtor or lends money to pay off such debt does not entitle him to subrogation to the liens of the creditors so paid off. *McDonald, Shea & Co. v. Railroad*, 93 Tenn. 281; *Wood v. Guarantee Trust Co.*, 128 U. S. 416; *Morgan, etc., v. Texas Cent. R. Co.*, 137 U. S. 172; *Rhuling's Appeal*, 107 Pa. 161; *Sheldon on Subrogation*, § 243; *Unger v. Leiter*, 32 Ohio St. 210; *Griffin v. Proctor*, 14 Bush (Ky.), 571; *Fenner v. F. L. & T. Co.*, cited above.

"Conventional subrogation may result from a direct agreement between a debtor and a third person who pays the debt that he shall be subrogated to all the rights and securities existing in behalf of the creditor whose debt

45. *Browder & Co. v. Hill*, 14 A. B. R. 619, 136 Fed. 821 (C. C. A. Tenn.).

47. *In re Automobile Livery Serv-*

ice Co., 23 A. B. R. 799, 176 Fed. 792 (D. C. Ala.).

48. *In re Langley & Alderson*, 24 A. B. R. 69 (Ref. affirmed by D. C. Wis.).

is paid off. But nothing short of an express agreement to that effect will move a court of equity in behalf of such a creditor.

"A mere understanding upon the part of such a third person, under no obligations to pay the debt, that he, by such payment, will be subrogated to the liens of the creditor is not enough. *Sheldon on Subrogation*, §§ 243, 248, 250; 27 *Amer. & Eng. Ency. of Law*, 257; *Receivers of N. J. Ry. Co. v. Wortendyke*, 27 N. J. Eq. 658, overruling *Coe v. N. J. Ry. Co.*, 27 N. J. Eq. 111; *Unger v. Leiter*, 32 Ohio Stat. 210; *Brice v. Watkins*, 30 La. Ann. 21; *Hutchinson v. Rice*, 105 La. Ann. 471; *Cumberland B. & L. Ass'n v. Sparks*, 11 Fed. 648.

"Subrogation by agreement with the debtor alone to the equities and liens of a creditor whose debt is paid off by one under no obligation, is an equitable doctrine which comes from the civil law and is enforced only when the agreement creates equitable rights against the debtor which will not impair or overthrow equitable rights of the creditor or of innocent third persons.

"When therefore subrogation depends wholly upon an agreement with the debtor the rights of the creditor to the remainder of his debt must not be prejudiced. *Sheldon on Subrogation*, § 248 and §§ 70 and 127; 27 *Am. & Ency.* (2nd ed.), 257; *Bissett v. Gathone*, 67 Mo. App. 23, 26; *Stuckman v. Roose*, 147 Ind. 402; *Smith v. Morrison*, 29 S. W. 1116; *Fievel v. Zuber*, 67 Tex. 279.

"The evidence of a direct agreement between Browder & Co. and the Furnace Company that the lien in behalf of laborers should be kept alive, and appellant substituted thereto is not so clear and satisfactory as to justify a reversal of the finding against such an agreement by the referee and district judge.

"That both parties supposed that Browder & Co. would stand precisely in the shoes of the laborers who received orders on them for goods simply because the orders were given as credits upon current wages is not enough. It may have been of some convenience to the workmen to receive such orders in advance of one of the regular pay days, but it was a convenience for which they doubtless more than paid, for it appears that if they insisted upon money instead of goods a discount of from 15 to 25 per cent. was exacted. Neither was the scheme without profit to the debtor for the arrangement was that the Furnace Company should give credit for these orders on Browder & Co. only to the extent of 95 per cent. of their face value.

"So, too, if it did not suit the convenience of the Furnace Company to pay these orders when the wages of the men became due an ordinary promissory note was given in settlement or a mere credit was given upon the books for the aggregate of the orders presented. All of these circumstances tend to indicate that the ordinary relation of debtor and creditor existed and that the parties acted upon the erroneous idea that because the orders given were in partial payment of wages that the debt thus created would stand in the shoes of the debt paid off.

"Neither would be justified in reversing the order denying subrogation when it is evident that subrogation will prejudice the rights of the very laborers whose claims were only partially paid off by the goods supplied them upon the employer's order.

"The distinct stipulation is that the assets of the bankrupt, after paying expenses, will not pay labor claims proper in full if this substitution is allowed.

"Being a pure equity, subrogation by agreement with the debtor alone will not be accorded if it impair the security of the creditor for the remainder of his debt or prejudice innocent third parties having equities of equal rank."

§ 2280. Subrogation of Sureties for Bankrupt to Creditors' Rights and of Creditors to Indemnity Given Sureties.—Likewise, sureties for the bankrupt are entitled to subrogation, pro tanto, to the creditors' rights and indemnities; and creditors, on their part, are entitled to subrogation to indemnity given sureties for the debt.

Thus, a retiring partner is subrogated to the claim of a creditor which he has been compelled to pay;⁴⁹ and the trustee of one bankrupt partner may prove against the individual estate of the other partner the claim of an individual creditor of the other partner for which he was surety and which he has paid.⁵⁰ Creditors have right of subrogation to the indemnity given by the debtor to the surety.⁵¹

And of course a surety paying the bankrupt's debt is entitled to subrogation, pro tanto, to the creditor's claim and rights.⁵²

Thus a surety, upon payment, after bankruptcy, of the bankrupt's debt, may be subrogated to a valid attachment lien held by the creditor.

Mason v. Hurling, 11 A. B. R. 303, 143 Fed. 197 (D. C. Vt.): "In this case the whole current of authorities is that payment of a debt by a surety or endorser is considered to operate as an assignment of it, and the equity of subrogation has received a liberal and broad construction, dependent, however, upon the preliminary question of fact whether the payment was intended as a purchase or an extinguishment of the debt. If the former, the surety signer, as the purchaser, may be subrogated to all the rights of the original creditor."

Likewise, a surety paying a claim after the bankruptcy may be subrogated to the claimant's right to rescind the sale and reclaim the property.

Sessler v. Paducah Distilleries Co., 21 A. B. R. 723, 168 Fed. 44 (C. C. A. La.): "* * * it is also contended that, as Menard Bros. took no express subrogation at the time of payment, they acquired no rights of the original creditor to rescind the sale. There may be some doubt as to whether any subrogation took place by contract; but as Menard Bros. were sureties of David Brunner [the bankrupt], and paid the debt, we think they are legally subrogated under the Louisiana Code. * * * We have no doubt about the right of a surety to prosecute his claim in bankruptcy in the name of the principal creditor, when subrogation takes place after proof of debt."

And a wife, who has mortgaged her separate property for her husband's debt, will be subrogated to the creditor's claim on payment thereof.⁵³ Likewise, sureties paying their principals' debts in whole or in part are subrogated pro tanto, to the creditors' claims and right in the dividends.⁵⁴

Again, children who have surrendered to their father insurance policies for specific purposes, have been held subrogated, as sureties, where the

49. *In re Dillon*, 4 A. B. R. 63, 100 Fed. 627 (D. C. Mass.).

50. *In re Mason & Son*, 2 A. B. R. 60 (Ref. R. I.).

51. *In re Printing Co. v. Brew Co.*, 4 A. B. R. 183, 101 Fed. 699 (C. C. A. Ky.).

52. See ante, § 613.

53. *In re Carter*, 15 A. B. R. 126, 138 Fed. 846 (D. C. Ark.).

54. See ante, subject of surety's claims, § 613.

proceeds of the policies have been misapplied to the extinguishment of liens.⁵⁵

§ 2281. Subrogation of Interested Party, Paying to Preserve Assets.—Where one, not a volunteer but interested in the bankrupt's business or in the property involved, pays a claim in order to preserve or protect the business or property, the claim is not necessarily extinguished, but he may be subrogated to the rights of the claimant.

Thus, a remainderman furnishing money to pay taxes to a bankrupt life tenant, who has been collecting rents after the bankruptcy, the trustees in bankruptcy having successively resigned, is entitled to reimbursement out of the bankrupt estate.⁵⁶

And the doctrine of subrogation will be applied whenever a person, not a mere volunteer, pays a debt or demand, which, in equity and good conscience, should have been satisfied by another.⁵⁷

This doctrine has been applied in favor of a partner who had sold out but had failed to notify creditors of the dissolution of the firm, and who was subsequently jointly sued on a debt contracted by the remaining partner after the dissolution, and who had left security with the sheriff to pay the execution in case the remaining partner could not be made to pay it; the court holding the judgment was not "paid," though originally marked so by the sheriff, but was still alive as against the trustee in bankruptcy of the remaining partner.⁵⁸

Thus, again, where the owners of logs paid off workmen's liens, in order to prevent foreclosure, the employers of the workmen having become bankrupt, the log owners were held entitled to subrogation to the workmen's liens.⁵⁹

So, an assignee for the benefit of creditors, who has redeemed a pledge, will be entitled to a claim against the estate for the amount advanced by him.⁶⁰

§ 2282. Mere Volunteers Not Entitled to Subrogation.—But a mere volunteer, not interested in the property involved nor acting in pursuance of an agreement for subrogation, is not entitled to subrogation.

Thus, as to the purchaser of a tax title, where a city, after filing a claim for unpaid taxes upon the real estate of a bankrupt, sold under mortgage foreclosure in the state court free of all taxes (the state court refusing to order the taxes paid from the proceeds because the Bankruptcy Act was

55. *In re MacDougall*, 23 A. B. R. 762, 175 Fed. 400 (D. C. N. Y.).

56. *In re Force*, 4 A. B. R. 114 (Ref. Mass.). As to reimbursement for taxes paid and subrogation to tax liens paid off, see ante, § 2149.

57. *In re Bruce*, 19 A. B. R. 770, 158 Fed. 123 (D. C. N. Y.).

58. *In re Bruce*, 19 A. B. R. 770, 158 Fed. 123 (D. C. N. Y.).

59. *Obiter*, *In re Langley & Alderson*, 24 A. B. R. 69 (Ref. affirmed by D. C.). This case is obiter, because it was held that the transferring of the time checks created an actual assignment.

60. *In re William W. Rudd*, 25 A. B. R. 35, 180 Fed. 312 (D. C. N. Y.).

thought to require priority of payment thereof from the personal estate of the bankrupt) sells the property for the unpaid taxes as provided by statute, the purchaser at the tax sale was held not to be entitled to subrogation to the city's right of priority of payment from the bankrupt estate.

In *re Brinker*, 12 A. B. R. 125, 128 Fed. 634 (D. C. N. Y.): "Nor does the principal of the right of equitable subrogation have application here. * * * The purchasers of the tax certificates were not obliged to bid in the property at the tax sale in order to protect themselves. They were not mortgagees or judgment creditors, or even creditors, of the bankrupt. They are third parties to the transaction, pure and simple, and accordingly cannot invoke the aid of the doctrine of subrogation."

Thus, also, the paying of a bankrupt corporation's pay roll, but with no understanding for subrogation, either with the corporation or the workmen, and without present pecuniary interest, does not entitle to subrogation.⁶¹

§ 2283. No Subrogation of Trustee to Liens on Exempt Property Paid Off on Eve of Bankruptcy.—No right of subrogation to liens on exempt property paid off by the bankrupt on the eve of bankruptcy exists in favor of the trustee.⁶²

DIVISION 7.

PROCEDURE ON DISTRIBUTION.

§ 2284. Distribution to Be Based on Order of Court.—The trustee should make no distribution without first obtaining an order of the court. Where there are partnership and individual assets and liabilities for administration, the marshaling of the estates is to be based upon an order of the court. Likewise, priority claims are not to be paid until allowed and ordered paid by the court. Dividends are not to be paid until declared and ordered paid by the court.

There seems to be no set form of procedure for bringing about these orders of distribution. Undoubtedly, a formal motion would be proper, although in practice it is not customary. Usually the order marshaling the estates, where partnership and individual estates are being administered in one bankruptcy, and the order declaring a dividend, are made upon oral motion, generally at the coming on of the hearing upon the trustee's report.

⁶¹ In *re Taft*, 13 A. B. R. 417, 133 Fed. 511 (C. C. A. Ohio). Unreported case *Theobald v. Hammond* (decided as case No. 1239, C. C. A. Ohio).

⁶² *Obiter*, In *re Wilson*, 10 A. B.

R. 524, 123 Fed. 20 (C. C. A. Calif.); *obiter*, *Southern Irr. Co. v. Wharton Nat. Bank*, 28 A. B. R. 941 (Civ. App. Tex.); *contra*, In *re Boston*, 3 A. B. R. 388, 98 Fed. 587 (D. C. Neb.).

SUBDIVISION "A."

TRUSTEE'S REPORTS AND MEETINGS OF CREDITORS TO CONSIDER THEM.

§ 2285. **Trustees' Reports.**—The first step in practice towards the distribution of the assets is the filing by the trustee of one of the reports required by the statute and Supreme Court's General Orders to be filed by him from time to time as part of his duties.

It is one of the statutory duties of the trustee to report to the court, in writing, the condition of the estate and the amount of money on hand, and such other details as may be required by the court, within the first month after his appointment and every two months thereafter, unless otherwise ordered by the court.⁶³

§ 2286. **Form of Trustee's Reports.**—The form of trustee's report prescribed by the Supreme Court, known as Official Form No. 49, should be followed with such alterations as may be necessary to suit the particular case.⁶⁴

This form, like the other prescribed forms, is merely directory and need not be followed where the facts of the case require variation from them.⁶⁵

And here it might properly be remarked that these official forms, while indicative of the supreme court's interpretations of the statutory provisions and thus valuable in aiding in the interpreting of the statute, are not to be absolutely followed, in all events, but may be altered to suit the circumstances of each case. Indeed, the last order of the Supreme Court's General Orders in Bankruptcy, Order No. 38 itself, expressly states that:

"The several forms annexed to the General Orders shall be observed and used, with such alterations as may be necessary to suit the circumstances of any particular case."

In practice the trustee does not attempt to follow the prescribed form, No. 49, in making his reports and particularly in making the report that is preliminary to a distribution of the assets.⁶⁶

The report made at this stage of the proceedings usually states the amount of money on hand; the amount still likely to come in; the expenses incurred thus far in the administration of the estate and those that are likely to be incurred therein in the future; the costs of the court's officers, their fees, expenses and commissions; the disbursements already ordered by the court; the several amounts claimed by creditors who claim to have priority of payment out of the fund, and the several amounts claimed by

63. Bankr. Act, § 47 (10). See ante, § 917.

64. Official Form No. 49.

65. See ante, § 26.

66. But see *In re Carr*, 8 A. B. R. 636, 116 Fed. 556 (D. C. N. Car.), where the court says: "They (meaning the referees, trustees and deposi-

tories) must regard the rules as prescribed by the Supreme Court in the general orders and by this court in the district rules. * * * These rules are made for a purpose which they serve only when observed." Also, see ante, § 26.

general creditors who are without priority; the report usually ending or being accompanied with a request that the court allow the trustee his expenses, tax the fees and costs and commissions, determine the validity and priority of claims and order them paid in the order of their priority, and finally declare a dividend to creditors.

§ 2287. Review of Order Approving Trustee's Report and Allowing Expenses and Commissions.—The order approving the trustee's report, allowing expenses and commissions and declaring a dividend may be reviewed.⁶⁷

§ 2288. If Meeting Called to Consider Report, Ten Days Notice Requisite.—If a meeting of creditors is called to consider the report, ten days notice by mail must be given to all creditors, unless they have waived the notice in writing.⁶⁸

§ 2289. Also, if Dividend to Be Declared.—If a dividend is to be declared, ten days notice thereof likewise must be given.⁶⁹

§ 2290. Contents of Notice.—The notice need not state the items of expenses or the particular amounts of the various applications for allowance of attorneys' fees, etc., to be considered, but it is good practice to state in the notice as much of this kind of information as is feasible, for in this way creditors are kept informed of the progress of the estate, and oftentimes a wholesome corrective influence is exercised against exorbitant charges and extravagant allowances for attorneys' fees and other expenses.

§ 2291. Auditing of Accounts.—It is the duty of the referee in charge to audit the accounts of the trustee,⁷⁰ also that of the receiver.⁷¹ And it is the referee's duty to closely scrutinize the accounts, whether exceptions are filed or not.⁷²

§ 2292. At Time and Place Set, Report to Be Passed on, Expenses Allowed, Dividends Declared and Distribution Ordered.—At the time and place set in the notice, it is usual to approve or disapprove the report, in whole or in part, allow the expenses of the officers

67. In re Scherr, 14 A. B. R. 794 (D. C. Pa.). See post, § 2839, et seq., "Appeal and Review."

68. Bankr. Act, § 58 (a): "Creditors shall have at least ten days notice by mail, to their respective addresses as they appear in the list of creditors of the bankrupt, or as afterwards filed with the papers in the case by the creditors, unless they waive notice in writing of * * * all meetings of creditors." Also, see ante, § 565.

69. Bankr. Act, § 58 (a) (5). See ante, § 565.

70. Gen. Order No. XVII: "All accounts of trustees shall be referred as of course to the referee for audit, unless otherwise specially ordered by the court." Bankr. Act, § 62. Also, see ante, § 517.

71. Impliedly, In re Reliance Storage & Warehouse Co., 4 A. B. R. 49, 100 Fed. 619 (D. C. Pa.). See ante, § 518.

72. In re Baginsky, 2 A. B. R. 243 (Ref. La.). See ante, § 517.

of the court and their fees, allow claims of creditors, including those entitled to priority of payment, declare a dividend and order distribution.

§ 2293. **Exceptions to Reports and Orders of Distribution.**—Of course, exceptions may be taken by parties in interest, to the approval of the reports, and the allowance of expenses and fees and to the order of distribution.⁷³

But the creditor desiring to take such exception must act with due diligence, and laches may be fatal.⁷⁴

§ 2294. **Exceptions to Accounts to Be Filed Promptly.**—Exceptions to the receiver's or trustee's account should be filed promptly. They do not come under General Order 21, paragraph 6, relative to the re-examination of claims.⁷⁵

§ 2294¼. **And to Be Verified.**—And the exceptions should be verified.⁷⁶

§ 2294½. **Surcharging Accounts for Misconduct.**—A receiver's account has been surcharged with part of the loss occasioned by his carelessness in continuing to conduct business at a steady loss, where his books were improperly kept, funds commingled and the management left in the hands of the bankrupt's officers.⁷⁷

73. Instance, *In re Kyte*, 19 A. B. R. 768, 158 Fed. 121 (D. C. Pa.).

74. Instance, *In re Carothers & Co.*, 27 A. B. R. 603, 192 Fed. 691 (D. C. Pa.).

75. *In re Reliance Storage & Warehouse Co.*, 4 A. B. R. 49, 100 Fed. 619 (D. C. Pa.).

Exceptions to distribution—Practice as to time of filing. *In re Heebner*, 13 A. B. R. 256, 132 Fed. 1003 (D. C. Pa.).

76. *In re Ketterer Mfg. Co.*, 19 A. B. R. 646, 156 Fed. 719 (D. C. Pa.).

77. *In re Consumers' Coffee Co.*, 20 A. B. R. 835, 162 Fed. 786 (D. C. Pa.).

CHAPTER XLII.

CLOSING AND REOPENING OF ESTATES.

Synopsis of Chapter.

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- § 2315. Reopening Does Not Toll Year's Limitation for Proof of Claims.

DIVISION 1.

CLOSING OF ESTATES—FINAL MEETING.

§ **2295. Final Report and Final Meeting.**—If no appeal or error proceedings are pending, the final dividend is declared, the trustee's final report filed, the final meeting of creditors held and the estate closed and the trustee discharged of his trust.¹

1. A final settlement of the bankrupt's estate will not be ordered until a full and complete record of the proceedings is made, showing that they have been conducted in accordance with the requirements of the statute and the General Orders of the Supreme Court and the district court rules, and a balance sheet is presented which can be

understood and from which the bankrupt and his creditors can see what has been done with their money. In re Carr, 8 A. B. R. 635, 116 Fed. 556 (D. C. N. Car.).

It has been held, that a final dividend may be declared at a final meeting. See ante, § 2211.

§ 2296. Ten Days Notice of Final Report and Final Meeting.—Ten days notice by mail must be given of the final meeting of creditors, to all creditors except those who have waived notice in writing.²

§ 2297. Trustee's Duty to File Final Report.—It is the trustee's duty to lay before the final meeting of the creditors a detailed statement of the administration of the estate, and to make the final report and file the final account with the referee fifteen days before the day fixed for the final meeting of the creditors.³

And the trustee may be in contempt for failure to obey an order requiring him to file a final account.⁴

§ 2298. Estate Closed by Order Approving Trustee's Report and Discharging Trustee from His Trust.—Upon approval of the final account and report the trustee is discharged of his trust and the estate is closed, an order to this effect being entered.⁵

It is by the holding of such final meeting and the entry of such order of approval that the closing of the estate is technically effected.⁶

Clark v. Pidcock, 12 A. B. R. 315, 129 Fed. 745 (C. C. A. N. J.): "The estate, however, was not technically closed because there was no final meeting of creditors or discharge of a trustee upon the settlement of his accounts."

§ 2299. Certifying to Referee's Record and Transmitting to District Clerk.—The referee thereupon certifies to his record and transmits it to the district clerk, along with all the files; which thereafter are filed and remain the record and files of the bankruptcy court in that case.⁷

DIVISION 2.

REOPENING OF ESTATES ONCE CLOSED.

§ 2300. Jurisdiction to Reopen Estates.—The bankruptcy court has jurisdiction to reopen estates once closed, whenever it appears they

2. Bankr. Act, § 58 (a): Ten days notice, etc., must be given of "(6) the filing of the final accounts of the trustee, and the time, when and the place where they will be examined and passed upon."

3. Bankr. Act, § 47 (7) & (8). See ante, § 517.

4. *Obiter*, *O'Connor v. Sunseri*, 26 A. B. R. 1, 184 Fed. 712 (C. C. A. Pa.).
Judge Making Conditional Order of Commitment in Effect Extending Time May Necessitate New Contempt Proceedings.—*O'Connor v. Sunseri*, 26 A. B. R. 1, 184 Fed. 712 (C. C. A. Pa.).

5. Where the referee refuses to vacate an order discharging the trustee, so that creditors may file exceptions to the final account, the order having been en-

tered after ten days notice by mail to all creditors and in default of objections from any of them, nevertheless the district court has power to vacate the order. *Brown v. Persons*, 10 A. B. R. 416 (C. C. A. N. J.).

6. Section 2 gives the bankruptcy court jurisdiction to "(8) close estates whenever it appears that they have been fully administered, by approving the final accounts and discharging the trustees; and reopen them whenever it appears they were closed before being fully administered." In *re Stein*, 1 A. B. R. 663, 94 Fed. 124 (D. C. Ind.).

7. Compare suggestions in *re Carr*, 8 A. B. R. 635, 116 Fed. 556 (D. C. N. Car.).

have not been fully administered.⁸

§ 2301. Only One Ground for Reopening—Lack of Full Administration.—And there is only the one ground for reopening an estate, namely, that it has not been fully administered.

In *re Paine*, 11 A. B. R. 354, 127 Fed. 248 (D. C. Ky.): "The power to reopen a case is given in one contingency only, namely, when it appears that the case was closed before being fully administered."

§ 2302. Duty of Court to Reopen on Proper Showing.—And it is the duty of the court to reopen estates once closed, whenever sufficient proof is made that they have not been fully administered.⁹

§ 2303. But Reopening, Matter of Sound Discretion.—It rests within the sound discretion of the court, in view of all the circumstances, to reopen a case because of the estate not being fully administered.¹⁰

Simply that the bankrupt has been denied a discharge, and creditors may pursue him on old debts, will not cause the refusal of an application to reopen the estate. The creditors may pursue the assets through the machinery of the bankruptcy court if they so desire.¹¹ And no reopening will be granted on application of the bankrupt eighteen months after his discharge, where no assets exist and the only object is to make a creditor a party to attempt to bar him by the discharge.¹²

§ 2304. What Is Lack of "Full" Administration.—It has been held that the existence of assets unadministered must be shown;¹³ but probably there may be other lack of "full administration" that might authorize a reopening.¹⁴

§ 2305. No Time Limited for Application to Reopen.—No time is fixed by statute within which the reopening must be applied for or made.¹⁵

8. Bankr. Act, § 2 (8). In *re Newton*, 6 A. B. R. 52, 107 Fed. 430 (C. C. A. Mo.); In *re Paine*, 11 A. B. R. 354, 127 Fed. 248 (D. C. Ky.); impliedly, *Clark v. Pidcock*, 12 A. B. R. 309 (C. C. A. N. J.); impliedly, In *re Ryburn*, 16 A. B. R. 514, 145 Fed. 662 (D. C. Conn.); impliedly, In *re Barton's Estate*, 16 A. B. R. 569, 144 Fed. 540 (D. C. Ark.). Instance, *Traub v. Marshall Field & Co.*, 25 A. B. R. 410, 182 Fed. 622 (C. C. A. Ala.).

9. In *re Newton*, 6 A. B. R. 52, 107 Fed. 430 (C. C. A. Mo.).

10. In *re Paine*, 11 A. B. R. 351, 127 Fed. 248 (D. C. Ky.), where the application was made on the ground that the bankrupt had concealed assets.

In *re Goldman*, 11 A. B. R. 707, 129 Fed. 212 (C. C. A. N. Y.), also to recover concealed assets.

Inferentially, In *re Newton*, 6 A. B. R. 52, 107 Fed. 430 (C. C. A. Mo.); In

re Soper & Slada, 1 A. B. R. 193 (Ref. N. Y.).

11. In *re Barton's Estate*, 16 A. B. R. 576, 144 Fed. 540 (D. C. Ark.).

12. In *re Spicer*, 16 A. B. R. 802, 145 Fed. 431 (D. C. N. Y.).

13. In *re Newton*, 6 A. B. R. 52, 107 Fed. 439 (C. C. A. Mo.).

14. See, by way of suggestion, although contra, In *re Soper & Slada*, 1 A. B. R. 193 (Ref. N. Y.).

District court's simple order affirming a referee's order denying an application to reopen a case must be taken to affirm the referee's findings of fact that there were no unadministered assets. In *re O'Connell*, 14 A. B. R. 237, 137 Fed. 838 (C. C. Mass.).

15. In *re Paine*, 11 A. B. R. 354, 127 Fed. 248 (D. C. Ky.). Not directly in point but inferentially, *Clarke v. Pidcock*, 12 A. B. R. 309 (C. C. A. N. J.): "We do not see that any lapse of time,

§ 2306. But Must Be within Reasonable Time: Laches Will Bar.—The application for the reopening must be made within a reasonable time;¹⁶ and laches will bar the right.

In *re Paine*, 11 A. B. R. 351, 127 Fed. 248 (D. C. Ky.): "Something is doubtless left to the sound discretion of the court upon a consideration of all the circumstances surrounding each case. It would not be supposed that the court would as readily reopen a case where the creditors knew all the facts and slept on their rights as where the concealment of assets was not only artful but was unknown to the creditors, and not discovered by them for a long period. I take the proper rule to be that a fairly reasonable time, under all the circumstances of a case, should be allowed, and that if the parties who had full knowledge delayed an unreasonable time to seek to reopen a case, their laches would authorize the court to refuse to do so. But neither the statute nor judicial discretion dictates any hard and fast rule in the premises."

Each case must be decided on its own facts.¹⁷ Thus, a case will not be reopened on the application of a creditor in order to let him come in and contest the bankrupt's claim to exemptions, where such creditor has been duly scheduled and has had due notice of the proceedings.¹⁸

Likewise, seven years after a bankrupt has been granted a discharge the proceedings in bankruptcy will not be re-opened for alleged fraudulent concealment of assets, upon the petition of an assignee of a judgment, verified only on information and belief, which fails to show what property was surrendered by the bankrupt or what representations were made in his schedules as to property surrendered by him or that any creditor was deceived as to the facts or when the alleged fraud was discovered.¹⁹

But, in a case where the referee had never even called a meeting of creditors in the original bankruptcy, and no trustee had ever been appointed, reopening was permitted after the lapse of nearly ten years.²⁰

§ 2307. Application Not a "Suit" within § 11 (d) Limiting "Suits" to Two Years.—The application to reopen a case, upon the ground that the proceedings were closed before the estate was fully administered, is not a "suit" within the meaning of § 11 (d), providing that suits shall not be brought by or against a trustee subsequent to two years after the estate is closed.²¹

or at all events, the time elapsed in the present case, can have the effect of taking away this discretion to appoint a trustee, conferred by the section quoted upon a court of bankruptcy."

Impliedly (where ten years had elapsed), In *re Pierson*, 23 A. B. R. 58, 174 Fed. 160 (D. C. N. Y.). But in this case the facts show that the referee had never called a meeting of creditors in the original bankruptcy.

Traub v. Marshall Field & Co., 25 A. B. R. 410, 182 Fed. 622 (C. C. A. Ala.).

^{16.} In *re Paine*, 11 A. B. R. 351, 127 Fed. 248 (D. C. Ky.).

^{17.} *Traub v. Marshall Field & Co.*, 25 A. B. R. 410, 182 Fed. 622 (C. C. A. Ala.).

^{18.} In *re Reese*, 8 A. B. R. 411, 115 Fed. 993 (D. C. Ala.).

^{19.} *Vary v. Jackson*, 21 A. B. R. 334, 164 Fed. 840 (C. C. A. Ala.).

^{20.} In *re Pierson*, 23 A. B. R. 58, 174 Fed. 160 (D. C. N. Y.).

^{21.} In *re Paine*, 11 A. B. R. 351, 127 Fed. 248 (D. C. Ky.).

§ 2308. **Procedure: Application to Be to Judge.**—Reopening is accomplished by an application to the district judge, who, if he approves the application, enters an order reopening the case and re-referring the case to a referee; who thereupon calls a new meeting of creditors for the election of a new trustee, and closes the estate again in the regular manner, when it has been finally fully administered.²²

§ 2309. **No Formality Requisite in Application.**—No particular formality is necessary in the application.²³

§ 2310. **But Not to Be Indefinite: Should Be Verified and Show Assets Unadministered or Other Lack.**—But the application should not be indefinite, and it should be supported by affidavit, and it should show assets unadministered.

In re Newton, 6 A. B. R. 52, 107 Fed. 429 (C. C. A. Mo.): "We do not wish to be understood as holding that the petition to reopen an estate once closed must be of any formal or technical character. Such is not necessary, and in the practical administration of the Bankruptcy Act is not advisable, but such petition must be either in itself, or in connection with supporting affidavits, of such persuasive character as to reasonably satisfy the court of the requisite jurisdictional fact, namely, that there are some assets belonging to the bankrupt which have not been administered. We are of opinion that the petition in this case, if treated as a proceeding to reopen the estate, was vitally defective, in that it failed to state any substantial or definite facts from which the court could reasonably find that there were assets to be administered."

Or, if not assets unadministered, then some other lack of due administration.²⁴

§ 2311. **Who May Apply: Only Creditors Who Have Proved or May Prove Claims, Competent.**—Only creditors who have proved, or are still entitled to prove, their claims may have the estate reopened. Thus, a former trustee is not a competent party;²⁵ nor is a creditor who did not prove his claim within the year after the adjudication;²⁶ but a creditor who filed his proof of claim within the year, although the estate was closed, is a competent party.²⁷ And the assignee of a claim that was duly proved

22. But compare, In re Sonnabend, 18 A. B. R. 119 (Ref. Mass.), where it is held, that the referee has the power to reopen the estate.

23. In re Newton, 6 A. B. R. 52, 107 Fed. 430 (C. C. A. Mo.).

24. In re Soper & Slada, 1 A. B. R. 193 (Ref. N. Y.).

25. In re Paine, 11 A. B. R. 351, 127 Fed. 246 (D. C. Ky.).

26. In re Paine, 11 A. B. R. 351, 127 Fed. 246 (D. C. Ky.); In re Meyer, 25 A. B. R. 44, 181 Fed. 904 (D. C. Ore.).

Contra, where no claims were originally filed, In re Pierson, 23 A. B. R. 58, 174 Fed. 160 (D. C. N. Y.). But this contra doctrine is not to be approved. The facts in the case, however, seem to disclose great laxity, if not irregularity, on the part of the referee in the original bankruptcy—he did not even call a meeting of creditors!

27. In re Paine, 11 A. B. R. 351, 127 Fed. 246 (D. C. Ky.), where the creditor filed his claim in the clerk's office within the year, the estate before the referee having been already closed.

within the year is a competent party, although the claim was not assigned to him until more than a year after the estate had been closed.²⁸

§ 2312. Who May Oppose Reopening.—It is questionable whether a bankrupt is competent to oppose the reopening of a case.

In *re Paine*, 11 A. B. R. 354, 127 Fed. 246 (D. C. Ky.): "Indeed, if a bankrupt has honestly surrendered all his assets to the trustee, he seems to have no interest in the question of reopening the case."

§ 2213. Whether Third Party Who Has Interests in Property Competent.—It does not appear to have been decided whether a third party who has an interest in the property is competent, either to apply for reopening or to oppose the reopening of an estate.

§ 2314. Trustee Elected Anew and Administration to Proceed in Usual Manner.—Upon the reopening of the estate a trustee must be elected, the old trusteeship not being revived by the reopening. And the court may not appoint a trustee unless the creditors have first been given an opportunity to do so and have failed to make choice.²⁹

In *re Newton*, 6 A. B. R. 54, 107 Fed. 429 (C. C. A. Mo.): "This section, in our opinion, confers upon the creditors of the estate the same authority and power with respect to the appointment of a trustee, after an estate once closed has been, by order of court, reopened, as is conferred upon them at the first meeting held after the adjudication."

The reopening of the estate effects no more than the putting of the estate back into process of administration. Steps must be taken, just as if the estate had never been closed; thus, the reopening of the estate on the ground of an alleged fraudulent conveyance is not in and of itself an authority to bring suit to set the conveyance aside.³⁰

Amendment of the schedules may be permitted to claim exemptions out of newly-discovered assets, provided the bankrupt has not been acting in bad faith.³¹

§ 2315. Reopening Does Not Toll Year's Limitation for Proof of Claims.—The reopening of the estate does not toll the statutory limitation of one year from the adjudication for the proof of debts; and subse-

28. Impliedly, *Clark v. Pidcock*, 12 A. B. R. 314, 129 Fed. 745 (C. C. A. N. J.).

29. Bankr. Act, § 44 (a): "The creditors of a bankrupt state shall at their first meeting * * * or after an estate has been reopened * * * appoint one trustee or three trustees of such state."

Inferentially, obiter, In *re Barton's Estate*, 16 A. B. R. 577, 144 Fed. 540 (D. C. Ark.). But compare procedure in *Clark v. Pidcock*, 12 A. B. R. 315, 129 Fed. 745 (C. C. A. N. J.).

30. In *re Ryburn*, 16 A. B. R. 514, 145 Fed. 662 (D. C. Conn.).

31. In *re Irwin*, 22 A. B. R. 165, 177 Fed. 284 (D. C. Pa.).

quent proceedings, so far as unsecured creditors are concerned, can only redound to the benefit of those who have filed their proofs of claim within the year after the adjudication.³²

32. *In re Shaffer*, 4 A. B. R. 728, 104 Fed. 431 (D. C. N. Car.).

Contra, where no claims were originally filed and no trustee originally appointed, *In re Pierson*, 23 A. B. R. 58, 174 Fed. 160 (D. C. N. Y.); but this doctrine is doubtful. The recounting, however, of the omission of the ordinary steps of the calling of a meeting of creditors, of the appointment of a trustee, etc., displays such a laxity of duty on the part of the bankruptcy referee as to imply an abandonment of the original bankruptcy.

Bankrupt's Former Attorney, Employed by Trustee to Collect Old Judg-

ment Obtained before Bankruptcy, No Lien for Fees Earned before Bankruptcy.—Where the bankrupt's attorney was employed by the trustee, on reopening the estate, to collect a claim on a judgment which the attorney had obtained previous to the bankruptcy, the attorney having presented no claim for attorney's fees for getting the judgment, there will be no lien on the amount recovered for the services rendered previous to the bankruptcy, the claim therefore having been discharged. *In re Blum*, 28 A. B. R. 60, 193 Fed. 304 (D. C. N. Y.).

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